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What's the Deal with Revlon?

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What's the Deal with *Revlon*?

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Under the Revlon *doctrine, courts are to apply a higher level of scrutiny in certain takeover situations in an attempt to control potential conflicts of interest that might prejudice target shareholders. However, the doctrine has always had sufficient "play in the joints" that one might reasonably wonder whether it has much of an effect in practice on short-term shareholder returns. Additionally, in recent years, the trend in Delaware's* Revlon *jurisprudence seems to be to defer to the target board as long as there are no glaring conflicts of interest. Taken together, these facts raise concern over the continued relevance of the* Revlon *doctrine.*

It turns out this concern is justified. In this Article, I present evidence that Revlon *has a significant effect on the type of sales process that target boards adopt—when in* Revlon *mode, they pursue active market checks with greater frequency, engage with more potential bidders and receive more bids. However, this difference in process has no discernible effect on shareholder returns, whether measured as abnormal market returns upon deal announcement or deal premia. And yet, there is still evidence, in this study and others, that conflicts of interest abound.*

In other words, the modern incarnation of Revlon *no long appears up to the task for which it was intended. Consequently, I argue that courts should reorient the doctrine around a robust review of the types of conflicts of interest that might actually harm target shareholders. Additionally, if as the Delaware Supreme Court has indicated, target shareholders might ratify the types of problems* Revlon *was intended to address through the mandatory statutory merger vote requirement, it will be necessary to adopt additional securities disclosure rules to provide shareholders with sufficient information to make an informed ratification decision.*

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INTRODUCTION

In the summer of 2011, BHP Billiton and Petrohawk Energy Corporation agreed to merge.[1] BHP, one of the world's largest mining companies, was at the time a gorilla of the industry with a market cap of over $100 billion. Petrohawk, by contrast, was a pygmy-sized player with a market cap of only $7 billion, and yet it owned the rights to some of the most important "shale plays"[2] in the world. For this reason, BHP viewed the transaction as giving it "greater exposure to the world's largest energy market, while also broadening [its] geographic and customer spread."[3] BHP agreed to pay $38.75 per share in cash, which valued Petrohawk's equity at about $12 billion.[4] This price represented a premium of 62% over the prevailing market price on the day prior to the deal's announcement.[5] Perhaps not surprisingly, given this premium, the market cheered the transaction. Upon deal announcement, Petrohawk's stock jumped by about 60% while BHP's was essentially unaffected.[6]

The price that BHP paid was not the result of a competitive bidding process. Petrohawk did not actively solicit any other bidders for the company, and in fact, it was barred from doing so by a month-long exclusivity agreement.[7] During that exclusivity period, no unsolicited bids emerged, and Petrohawk was able to increase BHP's original bid of $37.50 by only 3%.[8] The deal was structured as a two-step merger consisting of a tender offer for all Petrohawk shares, followed by a merger that would extinguish the remaining shares.[9] Under the merger agreement, Petrohawk was prohibited from actively soliciting any additional bids between the time of signing and closing,[10] a period that ended up lasting only one month.[11] Nevertheless, the agreement contained a standard fiduciary out, which would allow the Petrohawk board under certain circumstances to withdraw or change its

1. *BHP Billiton and Petrohawk Energy Corporation Announce Merger Agreement*, BHP (July 15, 2011, 10:00 AM), https://www.bhp.com/media-and-insights/news-releases/2011/07/bhp-billiton-and-petrohawk-energy-corporation-announce-merger-agreement [https://perma.cc/N7B8-Z7LK].

2. The term "shale play" refers to shale formations containing accumulations of natural gas. *See Shale Gas Glossary*, DEP'T ENERGY, https://www.energy.gov/sites/prod/files/2013/04/f0/shale_gas_glossary.pdf [https://perma.cc/KQX4-UZLX].

3. *BHP Billiton and Petrohawk Energy Corporation Announce Merger Agreement*, *supra* note 1.

4. *Id.*

5. This data is from Thomson Reuters' SDC Platinum Database. *SDC Platinum*, THOMSON REUTERS, http://financial.thomsonreuters.com/en/products/data-analytics/market-data/sdc-platinum-financial-securities.html [https://perma.cc/7XW3-RZTU].

6. *See id.*

7. Petrohawk Energy Corp., Offer to Purchase (Exhibit 99A.1.A to Schedule TO), at 27 (July 25, 2011) [hereinafter "Offer to Purchase"].

8. *See id.* at 27–28.

9. *See id.* at 11–13.

10. *See id.* at 38–39.

11. *BHP Billiton Completes Acquisition of Petrohawk Energy Corporation*, BHP (Aug. 26, 2011, 10:00 AM), https://www.bhp.com/media-and-insights/news-releases/2011/08/bhp-billiton-completes-acquisition-of-petrohawk-energy-corporation [https://perma.cc/P7EV-L9AM].

recommendation that the shareholders tender their shares.[12] Additionally, under the deal, Floyd Wilson, Petrohawk's sixty-three year old chief executive officer (CEO) and chairman of the board who negotiated the deal with BHP, was to receive $5 million in consulting fees for a six-month period following the closing of the deal.[13] These consulting fees represented about 142% of the cash portion of Wilson's salary for the entire prior year when he was serving as CEO of the company.[14]

Under Delaware law, a deal like the one between BHP and Petrohawk warrants what is referred to as *Revlon* scrutiny, a more searching form of judicial scrutiny than the extremely deferential business judgment review that typically applies to a board's business decisions.[15] Originally adopted by the Delaware Supreme Court in the case *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*,[16] the *Revlon* doctrine was meant to "prevent the conflicts of interest that arise in the field of mergers and acquisitions by demanding that directors act with scrupulous concern for fairness to shareholders."[17] For example, the $5 million in consulting fees paid to Wilson might accurately reflect the value BHP placed on possibly the most knowledgeable person on the planet on all matters related to Petrohawk's operations. On the other hand, it might simply represent a payoff in an effort to persuade Wilson to prevail upon the Petrohawk board to select BHP as a merger partner and forgo any active solicitation that might generate even higher bids.

Revlon's solution to this conflict of interest problem was to require target boards, in certain takeover situations, to act as "auctioneers" tasked with getting "the best price for the stockholders."[18] Initially, this auctioneering duty implied adopting a process that typically would entail an active solicitation of bids either before or after signing a merger agreement with an acquiror.[19] The original rhetoric also implied that in sorting among reasonably similar bids, the target was to select the deal with the highest price.[20]

Despite these early aspirations of the *Revlon* doctrine, over time the Delaware courts relaxed the doctrine, holding that target firms in *Revlon* mode do not actually have to accept the highest bid. More recently, the Delaware Supreme Court has signaled a willingness to defer to target boards in *Revlon* mode, provided that there

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12. *See* Offer to Purchase, *supra* note 7, at 39–40.

13. *See id.* at 48; *see also* Petrohawk Energy Corp., Executive Retention Agreement (Form 8-K, Exhibit 10.1), at 2–3 (July 20, 2011); Petrohawk Energy Corp., Consulting Agreement (Form 8-K, Attachment 1), at 2 (July 20, 2011).

14. *See* Petrohawk Energy Corp., Proxy Statement (Form DEF 14A), at 42 (Apr. 16, 2011).

15. *See, e.g.*, AM. BAR ASS'N. MERGERS & ACQUISITIONS COMM., MODEL MERGER AGREEMENT FOR THE ACQUISITION OF A PUBLIC COMPANY, at xxiv (2011) (comparing the business judgment rule and the *Revlon* standard of review).

16. 506 A.2d 173 (Del. 1986).

17. Barkan v. Amsted Indus., Inc., 567 A.2d 1279, 1286 (Del. 1989).

18. *Revlon*, 506 A.2d at 182.

19. *Barkan*, 567 A.2d at 1287 ("When the board is considering a single offer and has no reliable grounds upon which to judge its adequacy, this concern for fairness demands a canvas of the market to determine if higher bids may be elicited.").

20. In *Revlon* itself, the focus was on the "best price." *See Revlon*, 506 A.2d at 182. It was not until almost a decade later that the Delaware Supreme Court started talking about the "best value." *See* Paramount Commc'ns, Inc. v. QVC Network, Inc., 637 A.2d 34, 44 (Del. 1994).

are no glaring conflicts of interest.[21] Under the modern incarnation of *Revlon* jurisprudence, the consulting fee in the BHP-Petrohawk deal likely would not count as a conflict of interest. Instead, the courts appear to be looking for boards that do not consist of a majority of outside directors or where there is an obvious bias in favor of the winning bidder.[22]

For these reasons, there is a real possibility that the *Revlon* doctrine no longer does what it set out to do, which is to maximize short-term shareholder returns. That is not to say that target boards in *Revlon* mode no longer adopt what is at least on its face a more competitive sales process. That seems unlikely because of a combination of path dependence[23] and the strong norms that favor such process.[24] However, based on the increasingly deferential approach of the *Revlon* jurisprudence, it might be that such process simply fails to make a difference for shareholders. On the other hand, there is a robust finding in the mergers and acquisitions literature that cash consideration is highly positively correlated with measures of shareholder returns, including, for example, abnormal market returns upon deal announcement and merger premia.[25] Since cash consideration is one of the things that triggers *Revlon* scrutiny,[26] it is at least plausible that these studies are picking up, in part, the effect that a *Revlon* influenced process has on such measures of shareholder gains.

This Article attempts to sort out these issues. The Article seeks to test the continued relevance of *Revlon* by considering its effect on the sales process of those companies that find themselves in *Revlon* mode as well as the effect of this process on measures of short-term shareholder return, in particular, abnormal market returns upon deal announcement and merger premia. I present evidence that *Revlon* does indeed affect deal process—it is associated with a higher incidence of active solicitations of bidders (so-called "active market checks"), a greater number of contacts with potential bidders, and a greater number of bids.[27] However, these deal-process variables are not associated with higher short-term shareholder returns.[28]

In other words, the data presented here confirms what one might conclude based on a review of *Revlon*'s modern turn toward increasing board deference—*Revlon* no longer leads to greater shareholder returns, if it ever did. *Revlon*'s focus on process has ultimately affected the deal process, but not in a way that actually meaningfully benefits shareholders. The Article concludes with a policy proposal: that the courts re-emphasize the importance of an active sales process in their *Revlon* jurisprudence while at the same time applying a higher level of scrutiny to the types of conflicts of

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21. *See infra* notes 174–88 and accompanying text.

22. *See infra* notes 174–88 and accompanying text.

23. For a general sense of theories of path dependence, see Lucian Arye Bebchuk & Mark J. Roe, *A Theory of Path Dependence in Corporate Ownership and Governance*, 52 STAN. L. REV. 127 (1999).

24. *Cf.* Edward B. Rock, *Saints and Sinners: How Does Delaware Corporate Law Work?*, 44 UCLA L. REV. 1009 (1997) (arguing that Delaware law creates social norms for directors and officers).

25. *See infra* notes 124–28 and accompanying text.

26. *See infra* notes 87–93 and accompanying text.

27. *See infra* notes 138–43 and accompanying text.

28. *See infra* notes 143–49 and accompanying text.

interest that motivated the *Revlon* inquiry in the first place.[29] Additionally, the Article considers Delaware's recent endorsement of the shareholder vote as a way to address the conflict of interest concerns underlying *Revlon*.[30] It argues that the current securities disclosure environment is unequipped for this task, and it proposes several disclosure rules that would be required to make such shareholder ratification work effectively.[31]

The Article proceeds as follows: In Part I, I discuss the origins of *Revlon* and its modern incarnation. In Part II, I conduct an empirical analysis of the effect of *Revlon* on deal process and shareholder returns. In Part III, I discuss the policy implications of the results presented in Part II.

I. THE *REVLON* DOCTRINE: ITS ORIGINS AND EVOLUTION

Revlon[32] was a watershed moment in the development of Delaware corporate law because it was the first time that the Delaware courts articulated a unique standard of review for evaluating takeovers.[33] The case involved Ronald Perelman, a swashbuckling investor who had accumulated a profitable group of companies, including a mid-level jewelry store and a regional supermarket chain. The CEO of Revlon, a sophisticated Frenchman named Michel Bergerac, did not feel for Perelman's company, Pantry Pride, the same affection that Perelman reserved for Revlon. Nor did Bergerac seem to like Perelman himself all that much, which probably explains why he consistently rebuffed his advances.[34] After several unsuccessful overtures, Perelman finally made a hostile cash tender offer for Revlon at successively increasing prices.[35] The deal was to be financed with a combination of junk bonds along with the proceeds from the sale of various key Revlon assets. Thus, under Perelman's plan, Revlon was to be broken up.

In response, on the advice of Marty Lipton, the famed mergers and acquisitions (M&A) advisor and Revlon's legal counsel, Revlon adopted a number of antitakeover defenses, including a poison pill.[36] But they also sought out a "white knight" in the form of Ted Forstmann, a respected Wall Street financier and the head of the private equity firm, Forstmann, Little & Company.[37] The deal Revlon struck with Forstmann was for cash at a price that was only slightly higher than Perelman's outstanding bid (and lower than Perelman's ultimate bid) and included a no-shop provision as well as a lock-up option on various valuable Revlon assets at a bargain

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29. *See infra* notes 166–87 and accompanying text.

30. *See infra* notes 188–97 and accompanying text.

31. *See infra* notes 188–97 and accompanying text.

32. Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc, 506 A.2d 173 (Del. 1986).

33. Some might say that the origins of *Revlon* can actually be found in the *Smith v. Van Gorkom* case, which was decided the year before *Revlon*. *See generally* 488 A.2d 858 (Del. 1985) (holding that a target board that spent no more than a few hours considering a takeover bid negotiated by a retiring CEO who offered a price that was accepted without a counteroffer was grossly negligent in violation of its duty of care).

34. *See Revlon*, 506 A.2d at 176.

35. *See id*. at 177–78.

36. *See id.* at 180–81.

37. *See id.* at 178, 183–84.

basement price.[38] Forstmann also agreed to issue promissory notes in exchange for certain Revlon-issued notes whose holders had been threatening to sue the Revlon board ever since the notes had suffered a significant drop in value due to the board's waiver of an important restrictive covenant.[39] Finally, the deal with Forstmann would require Revlon to sell off several operating divisions.[40]

Perelman sued and was awarded a preliminary injunction by the Chancery Court, which was upheld on appeal by the Delaware Supreme Court.[41] The problem was not so much the deal protection devices that Revlon initially adopted to ward off Perelman's unwanted bid. Those devices were permissible under the proportionality review established in *Unocal Corp. v. Mesa Petroleum Co.*[42] Rather, the problem had to do with the no-shop and lock-up provisions that Revlon had granted Forstmann Little.[43] In the court's view, those provisions effectively ended bidding for Revlon since Perelman could not compete with those agreements in place.[44] The court thought that cutting off bidding was particularly problematic in a situation like Revlon's where it was inevitable that the company was going to be broken up (since both Perelman's and Forstman's financing plans required selling off certain key Revlon assets).[45] In that context, the court determined that "[t]he directors' role changed from defenders of the corporate bastion to auctioneers charged with getting the best price for the stockholders at a sale of the company."[46]

The *Revlon* opinion introduced a new standard of review, sometimes called enhanced scrutiny, that is applicable in the takeover context. This standard requires "(a) a judicial determination regarding the adequacy of the decision making process employed by the directors, including the information on which the directors based their decision; and (b) a judicial examination of the reasonableness of the directors' action in light of the circumstances then existing."[47] Thus, under *Revlon* review, directors bear the burden of showing that they are "adequately informed and acted reasonably," but they are not required to show that they made a perfect decision, only a reasonable one.[48]

Not long after *Revlon* was decided, it became clear that *Revlon* duties apply not only to situations like *Revlon* where there are multiple bidders vying for the same target but also to situations where there is a single bidder. For example, just three years after *Revlon*, the Delaware Supreme Court decided *Barkan v. Amsted*

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38. *See id.* at 178–79.

39. *Id.* at 178–79. The covenant prohibited the company from incurring debt or selling assets going forward and was meant as a means of warding off Perelman. *See id.* at 177.

40. *Id.* at 178–79.

41. *Id.* at 185.

42. 493 A.2d 946 (Del. 1985). Under *Unocal*, an anti-takeover mechanism was permissible as long as there was a legitimate threat to the corporation and the response (i.e. the anti-takeover mechanism) was proportionate to that threat. *Id.* at 955.

43. *Revlon*, 506 A.2d at 183–84.

44. *See id.* at 184–85.

45. *See id.* at 182.

46. *Id.* at 182.

47. Paramount Commc'ns, Inc. v. QVC Network, Inc., 637 A.2d 34, 45 (Del. 1994).

48. *Id.*

Industries, Inc.,[49] a case involving a management-led buyout of Amsted.[50] The plaintiff shareholders argued the Amsted board breached its duties under *Revlon* by agreeing to the management-led buyout without attempting to solicit any other bids and with no way of knowing whether the price that management was offering was the best they could get consistent with their obligation to act as auctioneers.[51] The Delaware Supreme Court disagreed that the board had breached its duties. They recognized that:

> When the board is considering a single offer and has no reliable grounds upon which to judge its adequacy, this concern for fairness [underlying *Revlon*] demands a canvas of the market to determine if higher bids may be elicited. When, however, the directors possess a body of reliable evidence with which to evaluate the fairness of a transaction, they may approve that transaction without conducting an active survey of the market.[52]

In the case of the management buyout of Amsted, no other bidder had emerged in the ten months between signing and closing.[53] Additionally, the price reflected certain tax advantages that were unlikely to accrue to any bidder other than management, and therefore the board had reason to believe that it was likely the best price they could get.[54]

The *Barkan* case did a good job illustrating the potential scope of *Revlon*—that it applies potentially to every merger, not just ones involving competing bids—but the same year the *Barkan* case was decided, the Delaware Supreme Court issued yet another *Revlon* opinion that hinted at the doctrine's limits. In *Paramount Communications, Inc. v. Time, Inc.*,[55] the issue was whether the Time board had breached its *Revlon* duties when, in an effort to prevent Paramount from breaking up its merger of equals with Warner Bros., Time altered the structure of the deal with Warner to avoid a shareholder vote by Time shareholders.[56] Paramount and certain Time shareholders brought an action seeking to enjoin the Time-Warner transaction, alleging, among other things, that *Revlon* required the Time board to seek the best price for the company's shareholders.[57] In other words, the Time board could not simply reject Paramount's bid.[58]

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49. 567 A.2d 1279 (Del. 1989).
50. *See id.* at 1281.
51. *See id.*
52. *Id.* at 1287 (citations omitted).
53. *Id.*
54. *Id.*
55. 571 A.2d 1140 (Del. 1989).
56. The original deal between Time and Warner was structured as a stock-for-stock merger of equals under which Time's issuance of stock in connection with the merger would trigger voting rights on the part of its shareholder pursuant to the rules of the New York Stock Exchange. Time subsequently modified the deal so that Time would acquire Warner in an all-cash merger financed by debt, a structure that would not require approval by Time shareholders. *See id.* at 1146–49.
57. *See id.* at 1142.
58. *See id.*

However, the Delaware Supreme Court denied the requested preliminary injunction on the ground that *Revlon* had not been triggered for the Time board. In doing so, it affirmed the chancery court's decision, although it did so for different reasons.[59] The chancery court had held that *Revlon* required a change of control,[60] but the original Time-Warner merger did not constitute a change of control because Time did not have a controlling shareholder before it signed its deal with Warner, and it would not have one after.[61] Rather, "control of the corporation existed in a fluid aggregation of unaffiliated shareholders representing a voting majority—in other words, in the market."[62] Recognizing that the chancery court's conclusion was supported by the record and correct as a matter of law, the Delaware Supreme Court nevertheless premised its decision on different grounds, "namely, the absence of any substantial evidence to conclude that Time's board, in negotiating with Warner, made the dissolution or breakup of the corporate entity inevitable, as was the case in *Revlon*."[63]

Thus, whereas *Barkan* suggested a highly capacious scope for *Revlon*, *Time* suggested a more limited one. Additionally, while *Revlon* itself suggested demanding auctioneering duties, the *Barkan* case suggested something comparatively less so. These cases, while only the tip of the *Revlon* iceberg, do a good job illustrating the variable nature of the doctrine. They also reflect the two overarching questions raised, and still not entirely resolved, by the *Revlon* inquiry: (1) when does *Revlon* apply? and (2) what does *Revlon* require? I explore these questions in greater detail below.

A. When Does Revlon *Apply?*

Surveying its takeover jurisprudence nearly eight years after the *Revlon* decision, the Delaware Supreme Court identified three scenarios where *Revlon* duties apply.[64] First, they apply "when a corporation initiates an active bidding process seeking to sell itself or to effect a business reorganization involving a clear breakup of the company."[65] Second, they apply "where, in response to a bidder's offer, a target abandons its long-term strategy and seeks an alternative transaction involving the breakup of the company."[66] Third, they apply "when approval of a transaction results in a sale or change of control."[67]

Why these triggers? What is the animating principle behind them? The best answer is that they have to do with conflicts of interest. This is, after all, the concern of the *Unocal* test, which applies to a company's anti-takeover related response to a

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59. *See id.* at 1150.

60. *See* Paramount Commc'ns Inc. v. Time Inc., Nos. 10866, 10670, and 10935, 1989 WL 79880, at *23 (Del. Ch. July 14, 1989).

61. *Id.* at *21.

62. *Id.* at *16.

63. *Time*, 571 A.2d at 1150.

64. Arnold v. Soc'y for Sav. Bancorp, Inc., 650 A.2d 1270, 1289–90 (Del. 1994).

65. *Id.* at 1290 (quoting *Time*, 571 A.2d at 1150).

66. *Id.* (quoting *Time*, 571 A.2d at 1150).

67. *Id.* (quoting Paramount Commc'ns Inc., v. QVC Network, Inc., 637 A.2d 34, 42–43, 47 (Del. 1994)).

perceived threat and which the Delaware Supreme Court views, along with *Revlon*, as part of a unified field of inquiry.[68] Additionally, the view that *Revlon* is primarily concerned with conflicts of interest is one shared by scholars,[69] as well as several federal courts who so opine when called upon to apply *Revlon* or related doctrines.[70]

Of course, conflicts of interest are a perennial issue in corporate law. Why should they be of particular concern in the takeover context? The answer is because they are ubiquitous and, in some ways, unavoidable in the takeover context. Consider two different examples: In Example 1, Acquiror A might want to keep Target CEO in the same position following the transaction and perhaps even elevate him to the board of the combined company, a more prestigious position than his current membership on the Target board. Acquiror B, by contrast, might plan to terminate CEO's employment as soon as the deal is closed. However, maybe Acquiror B values Target higher than Acquiror A because of greater synergies and is therefore offering a higher price for Target. Can we really trust the CEO to make the right decision here for the shareholders? If he prevails upon the board to accept Acquiror A's offer, when Acquiror B would put Target's assets to a higher use, then this would be inefficient from society's perspective. In Example 2, by contrast, maybe Target CEO prevails upon the board to accept Acquiror B's offer, thus avoiding the inefficient outcome, but this time because Acquiror B offers Target CEO a lucrative "transaction bonus," Target CEO does not negotiate as hard as he otherwise would, thereby leaving money on the table for the Target shareholders. This scenario would raise a distributional question as opposed to an efficiency one.

To be sure, we could complicate things further by adding facts that make it less clear Target should accept Acquiror B's offer in Example 1. For example, maybe Acquiror B is offering a higher price but there is greater uncertainty as to whether the deal with Acquiror B will close because of more complicated regulatory or antitrust issues. Or maybe it is not so obvious that the transaction bonus that Acquiror B offers Target CEO in Example 2 is a bad thing. For example, maybe the bonus is necessary to get Target CEO to relinquish his position, along with all of the status and perks that go along with it. But for now, let us stick with the more simplistic version of these scenarios where the conflict of interest leads to a sale that is not

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68. "[T]he general principles announced in *Revlon*, in *Unocal Corp. v. Mesa Petroleum Co.*, and in *Moran v. Household International, Inc.* govern this case and every case in which a fundamental change of corporate control occurs or is contemplated." *QVC*, 637 A.2d at 46 (quoting Barkan v. Amsted Indus., Inc., 567 A.2d 1279, 1286 (Del. 1989)) (emphasis omitted) (citations omitted).

69. *See, e.g.*, MICHAEL P. DOOLEY, FUNDAMENTALS OF CORPORATION LAW 577 (1995); Stephen M. Bainbridge, *The Geography of* Revlon-*Land*, 81 FORDHAM L. REV. 3277, 3281 (2013). *But see* Mohsen Manesh, *Defined by Dictum: The Geography of* Revlon-*Land in Cash and Mixed Consideration Transactions*, 59 VILL. L. REV. 1, 27–28 (2014) (arguing that *Revlon* is animated by a mishmash of policy concerns that go well beyond the simple potential for conflicts of interest).

70. *See, e.g.*, Southdown, Inc. v. Moore McCormack Res., Inc., 686 F. Supp. 595, 602 (S.D. Tex. 1988) (describing the related *Unocal* standard as asking "whether a fully informed, wholly disinterested, reasonably courageous director would dissent from the board's act in any material part").

shareholder value maximizing, either of the inefficient or efficient variety. Are these actually problems?

There are two different arguments that are sometimes deployed in this context to suggest that in most cases, the answer to this question is "no," these are not actually problems. First, one might argue that if conflicts of interest lead to an inefficient sale, as in Example 1, this is not really a serious concern because another acquiror will come along and recognizing these inefficiencies, will acquire the combined company and correct the problem. In other words, the argument is that the market for corporate control will solve the inefficient sale problem. Accordingly, some commentators suggest that maybe *Revlon* should only focus on situations where the market for corporate control cannot be expected to work as well.[71]

Second, one might argue that if conflicts of interest end up shortchanging Target shareholders, leaving money on the negotiation table, this really should be of little concern since diversified shareholders are just as likely to be invested in the Acquiror as the Target (and possibly both) and that therefore the relative gains and losses will average out over time. Armed with this argument, commentators argue that *Revlon* should therefore focus on situations where diversified shareholders cannot be expected to invest in the acquiror—for example, where the acquiror's stock is not publicly traded.[72]

These arguments are not without their problems. The market for corporate control is hardly the laissez-faire ideal imagined in these arguments, particularly now that *Unocal* review has basically devolved into business judgment review.[73] Nor is it entirely clear why we should privilege the hypothetical diversified investor, particularly in corporate law where, unlike in the securities law context, we are focused on particular corporations with a particular shareholder base. But perhaps the biggest problem with these arguments is that they describe a world that could not be more different from the way corporate law actually works in practice.

For example, let us say that the Board of X Corp., beholden for various reasons to the domineering Chairman, agrees to hire the Chairman's family members in a number of executive positions for which they are wholly unqualified and enters into extravagantly generous employment agreements with them. It is certainly true that the market for corporate control could theoretically address that problem if Y Corp. were to acquire X Corp., oust the Chairman, his cronies on the Board, and his family members and replace them with competent people who work for no more than the market rate. But this possibility would not prevent a court from applying the entire fairness test to determine, most likely, that the CEO violated his duty of loyalty in the absence of approval by a disinterested board or shareholders.[74]

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71. *See, e.g.*, Bainbridge, *supra* note 69, at 3292–93.

72. *E.g., id.* at 3310–11.

73. *See, e.g.*, James D. Cox & Randall S. Thomas, *Delaware's Retreat: Exploring Developing Fissures and Tectonic Shifts in Delaware Corporate Law*, 42 DEL. J. CORP. L. 323, 384 (2018) ("The Delaware Supreme Court's movement of *Unocal* in the direction of the traditional deferential business judgment rule . . . .").

74. "Entire fairness, Delaware's most onerous standard, applies when the board labors under actual conflicts of interest. Once entire fairness applies, the defendants must establish 'to the court's satisfaction that the transaction was the product of both fair dealing *and* fair price.'" *In re* Trados Inc. S'holder Litig., 73 A.3d 17, 44 (Del. Ch. 2013) (emphasis in original)

Similarly, what if the Board of Alpha Inc. enters into various contracts with Beta Inc., a company that was founded by a majority of the Alpha board, who still owns a significant share of Beta, and the contracts they negotiate are extraordinarily favorable to Beta?[75] From the perspective of the diversified shareholder, this should not matter because it is just as statistically likely for that shareholder to be an owner of the Alphas of the world as it is the Betas of the world and therefore the losses and gains will average out over time. But even though this is true, that will not prevent a judge from analyzing the transaction under the entire fairness test and, most likely, determine that the Alpha directors breached their fiduciary duties.

In other words, Delaware corporate law does not follow the logic of these economic arguments in any other context involving conflicts of interest. In no other context does it allow the possibility of the salutary effect of market forces eliminate the need for judicial review of conflicted transactions. Why this is so is beyond the scope of this Article, although one can speculate as to the reasons.[76] The point, however, is that if these arguments do not generally do any work in other areas of Delaware corporate law, it is not clear why they should do so in the takeover context.

Thus, to reiterate, *Revlon* appears to be primarily about conflicts of interest, and *Revlon*'s solution is to require the target board in takeover situations to be laser focused on maximizing the short-term equity value of the corporation. But if this is so, then how do we explain the three *Revlon* triggers mentioned previously, focused as they seem to be on corporate breakups and control transactions? The answer, I think, has to do with the fact that every sale of a company has the potential to be influenced by conflicts of interest. Yet, clearly, the Delaware Supreme Court did not want *Revlon* to swallow up all of takeover law, as evidenced by its attempt to cabin its applicability in cases like *Time*.[77] For this reason, the *Revlon* triggers seem to identify situations where it is reasonable to assume that (1) the risk of conflicts is particularly high or (2) the potential costs of not policing for conflicts are particularly high.

It is perhaps easiest to see this point in the context of the control transaction trigger, the third trigger identified above. A control transaction in this context is

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(quoting Cinerama, Inc. v. Technicolor, Inc., 663 A.2d 1156, 1163 (Del. 1995)). "Not even an honest belief that the transaction was entirely fair will be sufficient to establish entire fairness. Rather, the transaction itself must be objectively fair, independent of the board's beliefs." *Id.* (quoting Gesoff v. IIC Indus., Inc., 902 A.2d 1130, 1145 (Del. Ch. 2006)).

75. *Cf.* Sinclair Oil Corp. v. Levien, 280 A.2d 717 (Del. 1971) (holding that a corporation that manages a contract between its wholly owned subsidiary and majority-owned subsidiary in such a way as to divert value to the wholly owned subsidiary runs afoul of the entire fairness standard).

76. Such speculation might begin with the fact that fiduciary duties are technically owed to the corporate entity, not the shareholders. While in most cases we think about them as running to the shareholders, this is just a useful heuristic. The diversified shareholder argument might be one of those cases where this useful heuristic leads to confusion. As for the market for corporate control argument, it is certainly true that market forces can impose a powerful check on mismanagement. But these market forces are meant as complements to, not substitutes for, fiduciary duties. This fact appears all the wiser when one considers how the market for corporate control has changed over time.

77. 571 A.2d 1140 (Del. 1989) (holding that *Revlon* does not apply in a stock-for-stock merger where the acquiror does not have a controlling shareholder).

defined as a sale of a company to an acquiror that itself has a controlling shareholder.[78] It is likely that conflicts of interest are greater in a control transaction than in non-control transactions. This is because a controlling shareholder typically reaps a disproportionate share of the synergies created by a transaction and therefore has an enhanced incentive to pay off target officers and directors through side payments (lucrative consulting fees, transaction bonuses, and the like) to persuade them to make a deal with the acquiror. Some have made the additional suggestion that the conflicts of interest inherent in a control transaction are also shielded from the market for corporate control because the controlling shareholder can effectively rebuff any subsequent offers for the combined company.[79] It has also been pointed out that diversified shareholders will not be indifferent about the distribution of post-transaction gains between the target and acquiror where the acquiror has a controlling shareholder because a diversified shareholder cannot reap the disproportionate gains of a controlling shareholder. And therefore, it cannot be said that these gains and losses will average out over time.[80]

However, as discussed above, even assuming these arguments are correct,[81] this is not the way corporate law works, and therefore in my view these arguments do not really help us understand *Revlon*. But fortunately, we do not need them for that purpose because the fact that control transactions involve a control premium and non-control transactions do not (and therefore that control transactions involve a greater risk of side payments to the target's directors or officers) is a sufficient reason to distinguish between the two for the purposes of *Revlon*.

While *Revlon*'s control trigger might be relatively easily explained in this way as consistent with the concern for conflicts of interest, the same cannot be said of the other two triggers, which both seem to involve the breakup of the company.[82] Why would a sale or reorganization involving the breakup of the company be worthy of particular attention when conflicts of interest are at stake? The reason is not because such transactions are likely to involve an elevated risk of conflicts of interest as was true in the case of the control transaction trigger. Rather, here, the motivation underlying these triggers more likely has to do with a desire to identify situations where the costs of failing to police conflicts of interest are particularly high. In the

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78. *See* Paramount Commc'ns Inc. v. QVC Network Inc., 637 A.2d 34, 42 (Del. 1993).

79. *See, e.g.*, Bainbridge, *supra* note 69, at 3310.

80. *Id.* at 3310–11.

81. *See supra* notes 72–77 and accompanying text.

82. To be sure, it is not exactly clear what the relationship is between these two triggers. After all, it is not clear why a reorganization involving the breakup of the company (of the type described in the first trigger) would not cover the type of transaction described in the second trigger. And although the first trigger clearly covers a reorganization involving the clear breakup of the company, it is not obvious whether the active bidding process alone acts as a *Revlon* trigger or whether it too must involve the clear breakup of the company. *See* Bainbridge, *supra* note 69, at 3306. As discussed above, there is a plausible explanation for why one might want to address a transaction involving the breakup of the company—if one is trying to police conflicts of interests, it is not as clear why an auction on its own (in other words, one not involving a corporate breakup) is any more susceptible to conflicts of interest than any other M&A transaction. For this reason, I choose to read the clause involving the "breakup" language in the first trigger as modifying both the reorganization clause as well as the active bidding clause.

case of the company breaking itself up by selling its assets—whether as the result of a reorganization, active bidding process or alternative transaction pursued in response to a takeover bid—this is the last opportunity for the owners of the target's particular collection of assets to get the best price available for them. To paraphrase Vice Chancellor Lamb in a slightly different context, the directors must maximize present, not long-term, share value because for the present shareholders, there is no long term.[83]

This endgame justification is also consistent with the case law, including *Revlon* itself. There, Forstmann Little was proposing to take Revlon private,[84] and therefore it is likely that even under Bainbridge's view, *Revlon*'s intermediate scrutiny would apply. After all, whereas diversified shareholders will not normally care about purely distributional issues, they will when the acquiror is a private entity, like Forstmann Little, since by definition they cannot own stock in the acquiror. Additionally, under Bainbridge's view, we might not normally concern ourselves about inefficient sales resulting from conflicts of interest because the market for corporate control will take care of such things.[85] However, because Forstmann Little is a private acquiror, there is no opportunity for an efficient buyer to acquire Forstmann and Revlon. For these reasons, Bainbridge is likely to see no inconsistency between his theory and *Revlon*.

The only problem is that this was not the Delaware Supreme Court's reasoning in *Revlon*. It was not concerned with the fact that Forstmann Little was a private acquiror.[86] Rather, it was concerned that, given the inevitable breakup of the company, this was the last opportunity for the shareholders of the Revlon assets, as constituted at the time, to get the best price for those assets.[87] In other words, the court was focused on the inevitable breakup of the company, not the non-public status of the acquiror.[88] For that reason, I think that this endgame justification is a more precedentially consistent way of defending the breakup related triggers of *Revlon*.

With all of this said, I do not want to give the impression that these corporate breakup triggers are unusually important in the everyday world of M&A practice. They are not. Rather, the most common real-world situation to which *Revlon* applies includes the sale of control, as in *Paramount v. QVC*. The other situation—actually the most common situation—where *Revlon* applies is the scenario where the target is being acquired for cash or mostly cash.[89] To be sure, this scenario is not identified among the three triggers set forth above. Nevertheless, it is widely accepted by

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83. *See* TW Servs., Inc. v. SWT Acquisition Corp., Nos. 10427, 10298, 1989 WL 20290, at *7 (Del. Ch. Mar. 2, 1989) (footnotes omitted) (explaining why cash consideration triggers *Revlon*).

84. Forstmann Little was a privately held private equity firm. Adam Lashinsky, *How Teddy Forstmann Lost His Groove*, CNN (July 26, 2004), https://money.cnn.com/magazines/fortune/fortune_archive/2004/07/26/377149/index.htm [https://perma.cc/KX4Z-94HL].

85. *See* Bainbridge, *supra* note 69 at 3294–96.

86. In fact, the court never even mentions that Forstmann Little was privately owned. *See* Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173 (Del. 1986).

87. *See id.*

88. *See id.*

89. There is no clear line for determining what percentage of cash in a mixed cash-stock deal is necessary in order to trigger *Revlon*.

practitioners,[90] and supported by Delaware caselaw,[91] that *Revlon* applies in cash mergers. The question is why?

The stated rationale is questionable at best. That rationale is basically the endgame argument once again: in cash mergers, the target shareholders are being cashed out and thus, this is the last opportunity for these shareholders to get the best price for the target's collection of assets.[92] The problem with this argument though is that it simply does not stand up to scrutiny. At least in a situation where the acquiror is a publicly traded company, cashed-out target shareholders who wish to participate in getting the best price for the target's assets in the future can simply reinvest in the publicly traded acquiror which now also owns the target. Thus, although I disagree with commentators like Bainbridge that the endgame justification has no role to play in explaining the *Revlon* triggers—I think it is the only explanation of the breakup triggers—I agree with him that it makes no sense in justifying the comparatively more recent trend to apply *Revlon* to cash mergers.

Regardless of its justification, however, the fact that cash consideration triggers *Revlon* is at this point beyond dispute.[93] Along with the change of control trigger, the cash consideration trigger represents the most common reason for *Revlon*. For this reason, in the data section in Part II below, I will focus on these two triggers for determining to what transactions in our dataset *Revlon* applies.

B. What Does Revlon *Require?*

As the Delaware Supreme Court explained in the *Barkan* case and has reiterated many times since, "there is no single blueprint that a board must follow to fulfill its duties [under *Revlon*]."[94] Under *Revlon*'s reasonableness review, the court takes into account a number of considerations: whether there was a market check of any kind, either active or passive, and whether before or after the merger or acquisition agreement was executed;[95] the target board's knowledge of the company and its

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90. *See, e.g.*, AM. BAR ASSOC. MERGERS & ACQUISITIONS COMM., *supra* note 15, at xxiv ("[A]n acquisition transaction that is primarily a cash transaction will be subject to *Revlon* . . . .").

91. *See* Manesh, *supra* note 69, at 14 n.84 (collecting cases).

92. *See, e.g.*, TW Servs., Inc. v. SWT Acquisition Corp., Nos. 10427, 10298, 1989 WL 20290, at *6 (Del. Ch. Mar. 2, 1989) ("In the setting of a sale of a company for cash, the board's duty to shareholders is inconsistent with acts not designed to maximize present share value, acts which in other circumstances might be . . . justified by reference to the long run interest of shareholders. In such a setting, for the present shareholders, there is no long run.").

93. *See* LOU R. KLING, BRANDON VAN DYKE & EILEEN T. NUGENT, NEGOTIATED ACQUISITIONS OF COMPANIES, SUBSIDIARIES AND DIVISIONS § 4.04 (observing that in a cash deal "*Revlon* clearly applies").

94. Barkan v. Amsted Indus., Inc., 567 A.2d 1279, 1286 (Del. 1989); *see also* RBC Cap. Mkts., LLC v. Jervis, 129 A.3d 816 (Del. 2015); C&J Energy Servs., Inc. v. City of Miami Gen. Emps.' & Sanitation Emps.' Ret. Tr., 107 A.3d 1049 (Del. 2014); Lyondell Chem. Co. v. Ryan, 970 A.2d 235 (Del. 2009); Paramount Commc'ns Inc. v. QVC Network Inc., 637 A.2d 34, 42 (Del. 1994).

95. A "passive market check" refers to the target board's ability to consider alternative bids and the likelihood that such bids will materialize. In the period prior to signing the merger agreement, a robust passive market check will require a sufficient period of time before signing

industry;[96] the target's visibility in the particular industry and financial community, as evidenced, for example, by the level of its analyst following;[97] the course of negotiations between the target and acquiror, including whether there was a serious back-and-forth between the parties that resulted in a price representing a premium over market;[98] whether other terms of the agreement, individually or in the aggregate, have the effect of discouraging an interested party from making a superior proposal.[99] With respect to this last factor, other relevant contractual terms include breakup fees, which are payable by the target to the acquiror in the event that the deal fails to close for certain reasons;[100] "matching rights," a provision that gives the acquiror the ability to match a third party's superior bid in the post-signing phase;[101] and "lock-ups," provisions that give the acquiror stock or target assets, often at a significantly discounted price, which act as a concession prize in the event of a topping bid but also deter such bids in the first place.[102]

But although there might be no single blueprint, there is a common theme to the varied blueprints that exist: information. Whatever sales process the target board adopts under *Revlon*, they have to be able to demonstrate that they possess sufficient information to determine the company's value and appropriately evaluate competing bids. The *Barkan* court clearly thought that in most cases, such information was only obtainable by canvassing the market either prior to signing (by publicly inviting bids)

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and closing for alternative bids to emerge. In the period following the signing of the merger agreement, a robust passive market check will also require the contractual right on the part of the target board to talk to and share information with other bidders and withdraw or withhold their recommendation from shareholders to vote in favor of the merger. Usually this contractual right is structured as an exception, called a "fiduciary out," to a "no solicitation" or "no-shop" provision barring the target board from actively soliciting interest in the company. An "active market check" refers to the target board's active solicitation of bids for the company. For this to occur post-signing, the target board will typically need a "go-shop" provision, which specifically grants this right of solicitation.

96. *See, e.g.*, *In re* MONY Grp. Inc. S'holder Litig., 852 A.2d 9 (Del. Ch. 2004) (finding that the board acted reasonably even though it did not actively solicit bidders because it was financially sophisticated and had knowledge of the industry).

97. *See, e.g.*, *In re* Lear Corp. S'holder Litig., 926 A.2d 94, 123 n.22 (Del. Ch. 2007) (denying the plaintiff's *Revlon* claim in part on the basis that the target "is one of the largest corporations in the United States with deep analyst coverage").

98. *See, e.g.*, *In re* Bear Stearns Litig., 870 N.Y.S.2d 709, 732 (N.Y. App. Div. 2008) ("A satisfactory showing under Revlon has been made where, as here, the directors: were sophisticated and knowledgeable about the industry and strategic alternatives available to the company; were involved in the negotiation process and bargained hard; relied on expert advice; and received a fairness opinion from a financial advisor.").

99. *See, e.g.*, Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173 (Del. 1986).

100. *See, e.g.*, Thomas W. Bates & Michael L. Lemmon, *Breaking Up is Hard to Do? "An Analysis of Termination Fee Provisions and Merger Outcomes*, 69 J. FIN. ECON. 469 (2003); Micah S. Officer, *Termination Fees in Mergers and Acquisitions*, 69 J. FIN. ECON. 431 (2003).

101. *See, e.g.*, Fernán Restrepo & Guhan Subramanian, *The New Look of Deal Protection*, 69 STAN. L. REV. 1013 (2017).

102. *See, e.g.*, Steven M. Davidoff & Christina M. Sautter, *Lock-Up Creep*, 38 J. CORP. L. 681 (2013).

or after signing by way of a go-shop provision.[103] Nevertheless, the court made clear that this would not always be the case, although it "decline[d] to fashion an iron-clad rule for determining when a market test is not required."[104] At the same time, the court went out of its way to clarify that "[t]he situations in which a completely passive approach to acquiring such knowledge [that the shareholders are getting the best price] is appropriate are limited."[105]

And yet, *Barkan* ended up being just such a case. Recall that it involved a management led leveraged buyout where no buyers other than management emerged for a period of ten months.[106] Additionally, management's offering price reflected certain tax advantages accruing to management that were unlikely to be captured by any other bidders, which, combined with the company's declining earnings, served as a basis for the directors' view that no other deal would result in a better price.[107]

More recent cases have suggested that the situations where, in a single bidder context, a passive approach is appropriate are perhaps not as limited as *Barkan* had suggested. For example, in *C&J Energy Services, Inc. v. City of Miami General Employees' & Sanitation Employees' Retirement Trust*, the Delaware Supreme Court confirmed that an active market check, either pre- or post-signing (by means of a "go-shop provision")[108] is not required, even when the target board's knowledge of the market is less than "impeccable," although there must be time available for at least a passive market check.[109] In *C&J Energy Services*, there were four months between the signing date and the expected closing date, a factor that was important in the court's decision that the target board complied with their *Revlon* duties.[110]

Although it is difficult to generalize, prior to *C&J Energy Services*, most practitioners would probably have agreed that in order to minimize one's potential *Revlon* exposure, in the absence of a go-shop provision, it would be wise to pursue a pre-signing market check, preferably an active one, combined with a fiduciary out in the event the agreement contains a no-shop provision and a termination fee in the 3% range.[111] Because *Revlon* does not require the target board to pick a particular bidder, as long as the board follows this process, it will almost certainly satisfy the *Revlon*

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103. *See* 567 A.2d 1279, 1287 (Del. 1989) ("When the board is considering a single offer and has no reliable grounds upon which to judge its adequacy, this concern for fairness demands a canvas of the market to determine if higher bids may be elicited."). A "go-shop" provision is one that explicitly allows the target company to solicit bidders during a period of time between signing and closing, subject to certain conditions.

104. *Id.* at 1288.

105. *Id.* at 1287.

106. *See id.* at 1281–83.

107. *See id.* at 1287–88.

108. *See supra* note 103.

109. 107 A.3d 1049, 1070 (Del. 2014) (opining that a four- or five-month period between signing and closing was more than enough time for a serious bidder to express interest).

110. *See id.*

111. For example, in the ABA's 2017 Deal Points Study of Public Company Mergers, the average breakup fee was around 3% and the vast majority of deals contained fiduciary outs. Claudia K. Simon et al.,*Strategic Buyer/Public Target M&A Deal Points Study*, 2017 A.B.A. MERGERS & ACQUISITIONS COMM. STUDY 46, 88, https://www.americanbar.org/content/dam/aba/administrative/business_law/deal_points/2017_public_study.pdf.authcheckdam [https://perma.cc/7E8D-5BQC].

standard of reasonableness. Of course, in the wake of *C&J Energy Services*, it is possible that a target could adopt a far laxer process and still meet *Revlon*'s reasonableness standard.

Let us pause at this point and consider then what *Revlon* requires. As originally conceived, *Revlon*, where applicable, requires the target board to act as an auctioneer, selling the company for the highest price available.[112] This auctioneering duty implies a procedural and substantive component: in order to sell for the highest price available, one must adopt a process that will generate a menu of prices.[113] And then one must choose the highest price among this menu of options.[114]

However, as the doctrine has developed, both of these substantive and procedural requirements have been significantly watered down. On the substantive side of the ledger, courts since *Revlon* have backed off substantially from the apparent requirement to choose the best price.[115] In perhaps the clearest articulation of this evolved position, the Delaware Court of Chancery has said that *Revlon* does not require the target board to accept the offer of, or even negotiate with, a bidder solely because the bidder offers a higher price, provided there are legitimate reasons to prefer the original bid.[116] In *Family Dollar*, the chancery court held that the target was not required to negotiate with a bidder whose offer was, unlike the original bidder's, an all-cash offer and made at a price that was more than 7% greater than the original bidder's. The target's reason for preferring the original bid was that it was, in its determination, more likely to be approved by antitrust authorities.[117] This holding gives target boards enormous latitude in choosing among bidders.

To be sure, if two bids were identical in all respects other than price, it seems unlikely that the target board could choose the lower bid consistent with its *Revlon* duties. However, it is never the case that bids are identical. There will always be differences. The question will be whether the difference the target identifies is sufficiently important to justify choosing the lower bid. But the trend appears to be that in the absence of any obvious conflict on the target board, the courts will defer to the board.[118]

That brings us to the second component of what *Revlon* requires, the procedural component. Originally, in *Barkan*, the Delaware Supreme Court suggested that in most cases, *Revlon* will require a target board to conduct an active market check, either prior to or after entering into a merger agreement.[119] Subsequent courts interpreting *Barkan* concluded that under *Revlon*, the only situation where a target board could avoid an active market check was if it had an "impeccable knowledge of the company's business for the Court to determine that it acted reasonably."[120]

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112. 506 A.2d 173, 182 (Del. 1986).

113. *See* Barkan v. Amsted Indus., Inc., 567 A.2d 1279, 1286 (Del. 1989).

114. *See Revlon*, 506 A.2d at 182.

115. *See, e.g.*, Paramount Commc'ns Inc. v. QVC Network Inc., 637 A.2d 34, 44 (Del. 1993) (discussing the need to choose the bid with the "best value" instead of the "best price").

116. *See In re* Family Dollar Stores, Inc. S'holder Litig., No. 9985–CB, 2014 WL 7246436 (Del. Ch. Dec. 19, 2014).

117. *See id.*

118. *See infra* text accompanying notes 185–86.

119. *See* Barkan v. Amsted Indus., Inc., 567 A.2d 1279, 1286 (Del. 1989).

120. *In re* OPENLANE, Inc. S'holders Litig., No. 6849-VCN, 2011 WL 4599662, at *5

However, in *C&J Energy Services*, the Delaware Supreme Court rejected this interpretation of *Barkan* and, in what was either a highly creative reading of that case or a silent overturning of it, held that an active market check is not required "so long as interested bidders have a fair opportunity to present a higher-value alternative, and the board has the flexibility to eschew the original transaction and accept the higher-value deal."[121]

In other words, *Revlon* has evolved to a point where there is very little substantive review as long as the process is reasonable—courts do not generally police whether the target has selected the "best price" or even the "best value." Thus, as long as the target conducts a reasonable process, it might choose Bid A over Bid B even though Bid A is the lower price of the two. At the same time, what counts as a reasonable process has also been redefined in the target board's favor so that in some, if not many, cases, a target board might, consistent with *Revlon*, enter into a deal with the bidder without first running an active market check, as long as the breakup fee is reasonable and there is a sufficient amount of time between signing and closing for other bidders to emerge.[122] The question is whether these changes drain *Revlon* of its relevance. That is the question I take up in the next Part.

II. Empirical Analysis

A. Hypothesis: Whether Revlon *Duties Make a Difference*

Does *Revlon* actually increase short-term shareholder value? There are at least two reasons to believe that it does, one theoretical and the other empirical. The theoretical reason for why *Revlon* likely increases short-term shareholder value is that that is precisely what *Revlon*'s auctioneering duty was meant to do.[123] However, as explained in Part I, in recent years, the Delaware courts have pruned that duty back significantly such that *Revlon* now requires little more than a reasonable process, which itself requires even less auction-like value-maximizing behavior on the part of the target board than in the original articulation of the doctrine.[124]

Nevertheless, there is also a strong empirical reason to think that *Revlon*, despite these doctrinal developments, still serves to increase short-term shareholder value. A longstanding, robust finding in the M&A literature is that cash deals are better for shareholders than stock deals.[125] In fact, cash deals are better not just for shareholders of the target, but shareholders of the acquiror as well.[126] Additionally, deal premia

(Del. Ch. Sept. 30, 2011).

121. C&J Energy Servs., Inc. v. City of Miami Gen. Emps.' & Sanitation Emps.' Ret. Tr., 107 A.3d 1049, 1067–68 (Del. 2014).

122. *See id.*

123. *See supra* text accompanying notes 121–22.

124. *See supra* text accompanying notes 121–22.

125. *See* Eliezer M. Fich, Edward M. Rice & Anh L. Tran, *Contractual Revisions in Compensation: Evidence from Merger Bonuses to Target CEOs*, 61 J. ACCT. & ECON. 338 (2016); Ulrike Malmendier, Marcus M. Opp & Farzad Saidi, *Target Revaluation After Failed Takeover Attempts: Cash Versus Stock*, 119 J. FIN. ECON. 92 (2016); Andrei Shleifer & Robert W. Vishny, *Stock Market Driven Acquisitions*, 70 J. FIN. ECON. 295 (2003).

126. *See, e.g.*, Fich et al., *supra* note 125, at 352.

tend to be higher in deals that are primarily cash based.[127] It is not exactly clear why this is the case. There is some evidence that cash deals signal to the market that the target is undervalued,[128] although it is not clear why they should have a similar effect on the acquiror's abnormal market returns on deal announcement.

To be sure, none of these studies speculate, let alone test whether, this result has anything to do with *Revlon*. In fact, none of these studies exhibit any awareness of the existence of *Revlon*. Nevertheless, it does stand to reason that some of this "cash consideration effect" has something to do with the fact that cash deals tend to follow a different sales process because of *Revlon*, and that sales process is intended to maximize short-term shareholder returns. However, to test this hypothesis we would need to control for the target's sales process, something that none of these other studies do. This leads to our first prediction:

> Prediction 1: Deals subject to *Revlon* duties tend to make more frequent use of pre-signing active market checks, enter into a greater number of contracts, and receive a greater number of bids than non-*Revlon* deals.[129]

But does this *Revlon*-mandated sales process have any actual effect on short-term shareholder value? One might think so based on the stated goal of the doctrine and the M&A literature's finding that cash deals (which typically trigger *Revlon*) are correlated with higher target shareholder returns. On the other hand, the doctrine's recent de-evolutionary trend along with the M&A literature's ignoring of *Revlon*'s influence altogether might cause one to question the doctrine's practical relevance. These reasons lead to our second prediction:

> Prediction 2: The *Revlon* sales process does not affect merger premia or market abnormal returns.

B. Data

I begin with all of the M&A transactions in Westlaw's Practical Law database from 2009 to 2016, which is a total of 1253 deals.[130] As the chart below illustrates,

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127. *See, e.g.*, *id.* at 348; Malmendier et al., *supra* note 125, at 92.

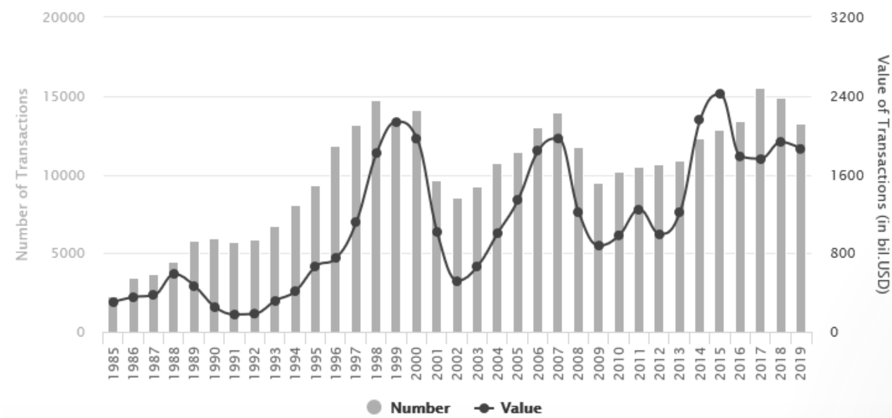
128. *See, e.g.*, Malmendier et al., *supra* note 125, at 92.

129. Recall that in *C&J Energy Services*, the Delaware Supreme Court held that *Revlon* does not require the active solicitation process implied by earlier precedent. C&J Energy Servs., Inc. v. City of Miami Gen. Emps.' & Sanitation Emps.' Ret. Tr., 107 A.3d 1049, 1067–68 (Del. 2014). However, that case was only decided in 2014. Consequently, I think it is safe to say that a sample of transactions that largely pre-dates this opinion should reflect that older precedent adopted a stronger presumption in favor of an active solicitation process.

130. A different period could have been selected. However, commentators have noted that the *Revlon* doctrine has evolved over time, with some suggesting that since the Delaware Supreme Court's decision in *Lyondell Chemical Co. v. Ryan*, 970 A.2d 235 (Del. 2009), the doctrine has not seemed to entail the enhanced substantive scrutiny implied by earlier opinions like *Paramount Commc'ns Inc. v. QVC Network, Inc.*, 637 A.2d 34, 44 (Del. 1994). *See* Lyman Johnson & Robert Ricca, *The Dwindling of* Revlon, 71 WASH. & LEE L. REV. 167, 172 (2014). Since this Article is primarily concerned with how the *Revlon* doctrine works now, I'm particularly interested in the post-*Lyondell* period. *Lyondell* was decided in 2009, and therefore

this period of time includes a slowdown for M&A activity in the wake of the financial crisis of 2007–2009, but it also includes the build-up to the M&A wave that we have experienced over the past couple of years. However, it excludes the significant M&A boom beginning in the early 2000s, which, combined with the fact that the *Revlon* doctrine might have worked differently during this time period,[131] might explain the slightly different results found by other papers.[132]

Chart 1: U.S. M&A Activity[133]



From this data set, I then pull relevant deal characteristics data from SDC Platinum for these transactions. I end up dropping about half of these transactions because of a lack of Compustat data for the target firm, which results in 697 deals. I drop forty of these observations because of a lack of Eventus data for these deals. Of the remaining 657 deals, I take a random sample of 290 of them to which I add hand-collected data from Securities and Exchange Commission (SEC) filings.

To test the two predictions outlined above, I am primarily concerned with two different sets of variables: First, there are the dependent variables, which consist of event study data (how the market reacts to announcement of the deal, as measured by abnormal returns) as well as market premium data (the premium that the deal price represents over the target's pre-announcement market price).

Second, there are the independent variables of interest, which are primarily the variables that deal with deal process: whether *Revlon* applied, whether the target pursued a pre-signing active market check, the number of contacts the target had with potential bidders, as well as the number of bids the target received. Of interest are also variables pertaining to the M&A agreement itself: the size of the breakup fee,

I chose that year as the starting point of our data.

131. *See* Johnson & Ricca, *supra* note 130, at 172.

132. *See* Matthew D. Cain, Sean J. Griffith, Robert J. Jackson, Jr. & Steven Davidoff Solomon, *Does* Revlon *Matter? An Empirical and Theoretical Study* (Eur. Corp. Governance Inst. – Law, Working Paper No. 466, 2019), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3418499 [https://perma.cc/CQJ8-M6X9].

133. *United States–M&A Statistics*, IMMA INST., https://imaa-institute.org/m-and-a-us-united-states/ [https://perma.cc/95JS-4ZTX].

the presence of a go-shop, the nature of the fiduciary out, and the number of days the acquiror has to match a potential superior offer by an interloping bidder. Additionally, there are variables that attempt to control for the presence of conflicts of interest at the target. These include whether the CEO received a payment, distinct from pre-negotiated parachute payments, in connection with the transaction—for example, a transaction bonus or a consulting agreement or the like. These variables of interest also include any post-closing positions that the CEO will hold at the combined company, whether the CEO is also the chairman of the target, and the number of years the CEO has before retirement (assuming a retirement age of sixty-five).

The other variables attempt to control for deal characteristics, including, for example, where the target and acquiror operate in different industries and whether the merger is a merger of equals, as well as various characteristics of the target, including, for example, asset size, operating cash flow and other financial metrics. All of these variables are summarized below in Table 1.

Table 1: Definition of Variables

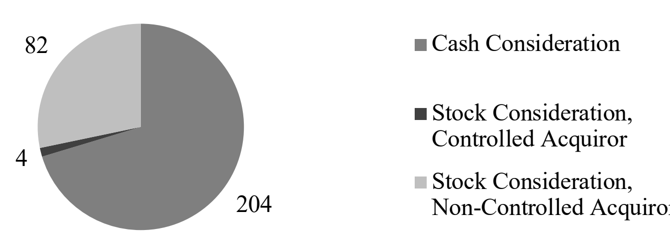
Conflict of Interest	**Source: SEC filings, except for CEO data, which comes from Execucomp**
Side Payment	One if the target CEO received some payment in connection with the transaction (e.g., transaction bonus, retention agreement, consulting agreement), zero otherwise
Post-deal Prestige Job	One if the target CEO is to be made the CEO of the combined company, the CEO of a subsidiary of the combined company or the chairman of the board of the combined company, zero otherwise
Post-deal Director	One if target CEO is to be made a member of the board of directors of the combined company (other than chairman of the board), zero otherwise
Post-deal employment	One if the target CEO will be a director or employee of the combined company following the transaction, zero otherwise
CEO Chairman	One if the target CEO is also the chairman of the target board, zero otherwise
Years to Retirement	The greater of zero and sixty-five minus the target CEO's age
M&A Agreement Data	**Source: Westlaw Practical Law**
Pro Acquiror Breakup Fee	Number of standard deviations the breakup fee is from the sample average of 3%, rounded to the nearest whole number, zero for any negative standard deviation
Pro Acquiror No Go-Shop	One if the transaction agreement contains a go-shop provision, zero otherwise

Pro Acquiror Fiduciary Out	One if the fiduciary out to the target board recommendation covenant is conditioned on a determination that (i) fiduciary duties require the board to not make the recommendation and (ii) the proposal is "superior", zero if it only requires determination (i)
Match Rights	One if the agreement contains a right for the acquiror to match a third party's offer that otherwise triggers the target board's fiduciary out
Days to Match	The number of days the acquiror has to match the third party's bid pursuant to the match right
Deal Process Characteristics	**Source: SEC filings**
Passive Market Check	One if the target conducted a passive market check (i.e., did not solicit bids), zero otherwise
Number of Total Contacts	The number of total prospective bidders, including the acquiror, the target talked to regarding a potential transaction
Bids	The number of bids, formal and informal, the target received from unique bidders, including the acquiror's (in other words, this number does not take into account the total number of bids any single bidder might have made)
Revlon	One if either the target is acquired for more than 50% cash or the acquiror has a controlling shareholder and the target does not
Target Initiated First Contact	One if the target was the first to contact the acquiror, zero otherwise
CEO Compensation	**Source: Execucomp**
CEO Stock Option Ownership	The value of the CEO's stock options
Deal Characteristics	**Source: SDC Platinum, except for the event study data, which is from Eventus**
Same Industry	One if both the target and the acquiror belong to the same forty-eight industry classification group
Tender Offer	One if the deal is structured as a tender offer, zero otherwise
Merger of Equals	One if the deal is classified as a merger of equal
Premium	Offer price to target stock price premium one day prior to announcement
Cumulative Abnormal Return (CAR)	The target's CAR over the window (-1,+1) around the merger announcement date, calculated as the residual from the market model estimated during the one-year window ending four weeks prior to the merger announcement

Target Characteristics	**Source: Compustat**
Size	The market value of the target's assets
Leverage	The target's book value of debt divided by the sum of book value of debt and market value of equity
M/B	The target's market value of equity divided by the book value of equity
OCF	The target's cash flow from operations scaled by the value of assets

Perhaps the most important variable is the *Revlon* variable, which measures whether *Revlon* applies to the transaction in question or not. As discussed in Part I, the two most common scenarios where *Revlon* applies is where the deal is for cash or where the acquiror is a controlled company and the target is not. For this reason, our *Revlon* variable is equal to one if either of these situations describes the deal in question and zero otherwise. Chart 2 below provides more information regarding the *Revlon* variable. About 208 deals, or about 72% of the deals in our sample, trigger *Revlon*. Of these deals, the vast majority are cash deals. In fact, only four of these 208 deals trigger *Revlon* solely because the acquiror is a controlled company and the target is not. Although twelve of the deals in our sample involve a controlled acquiror, eight of these are also cash deals, and thus they do not trigger *Revlon* solely because of the fact that the acquiror is a controlled company. Approximately 7% of all companies in the S&P 1500 are subject to a controlling shareholder,[134] and therefore our sample represents a smaller proportion of controlled acquirors (12/290, or 4%) than is in the general population.

Chart 2: Revlon Variable



Relevant summary statistics for other variables are set forth below in Table 2 below. According to Table 2, roughly 55% of the deals in our sample adopt an active pre-signing market check, which means that not every deal that triggers *Revlon* adopts an active pre-signing market check. This should not be all that surprising

134. Edward Kamonioh, *Controlled Companies in the Standard & Poor's 1500: A Follow-up Review of Performance & Risk*, INV. RESP. RSCH. CTR. INST. (Mar. 2016), https://www.weinberg.udel.edu/IIRCiResearchDocuments/2016/03/Controlled-Companies-IRRCI-2015-FINAL-3-16-16.pdf [https://perma.cc/SZA4-M5LX].

considering that the courts have never said that an active pre-signing market check is necessary, although in cases like *Barkan*, the Delaware Supreme Court signaled a strong preference for one.[135] Post-signing active market checks, by contrast, are relatively rare. Only about 5% of the deals in our sample employ a go-shop provision. This is slightly less than the percentage of go-shops in other studies.[136] In 31% of the deals in our sample, the target was the one to reach out to the initial bidder. The targets in our sample receive on average a total of two bids prior to signing the deal with the target, but the median is only one.

Although not reflected in Table 2, the average breakup fee, payable by the target to the acquiror in the event the deal does not close for certain reasons, is 3%, which is consistent with practitioner advice about what is "market" with respect to breakup fees.[137] Interestingly, the vast majority of the fiduciary outs have a particular formulation that favors the acquiror by making it more difficult for the target to exploit; the formulation being a fiduciary out conditioned on a determination that (i) fiduciary duties require the board to not make the recommendation and (ii) the proposal is "superior."

With respect to conflicts of interest, the CEOs in our sample are relatively young, approximately fifty-five on average; roughly 42% of these CEOs are also the chairman of the board. Additionally, 50% of the CEOs in our sample receive some sort of post-deal employment, with 33% receiving a post-deal "prestige" position, which, in this context, means becoming either the CEO or chairman of the combined company or remaining as the CEO of a subsidiary of the combined company (most likely the target).

Finally, with respect to the independent variables, the average deal price represents a 33% premium over the market price one day prior to the announcement of the deal. The market tends to like these deals on average, with positive abnormal returns of the combined target and acquiror. However, the market does not appear to like the price acquirors pay on average, as evidenced by the negative abnormal returns for acquirors. These statistics are consistent with the literature showing that acquirors tend to overpay in M&A transactions.[138]

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135. *See supra* notes 102–06 and accompanying text.

136. *See, e.g.*, Jin Q. Jeon & Cheolwoo Lee, *Effective Post-Signing Market Check or Window Dressing? The Role of Go-Shop Provisions in M&A Transactions*, 41 J. BUS. FIN. & ACCT. 210 (2014) (finding that out of 1706 transactions from 2004 to 2010, roughly 8% contained go-shops).

137. *See, e.g.*, MERGERS & ACQUISITIONS COMM., AM. BAR ASS'N, STRATEGIC BUYER/PUBLIC TARGET M&A DEAL POINTS STUDY 88 (2017).

138. *See, e.g.*, Laurence Capron & Nathalie Pistre, *When Do Acquirers Earn Abnormal Returns?*, 23 STRATEGIC MGMT. J. 781 (2002).

Table 2: Descriptive Statistics

Variable	**Proportion of Sample**	**Mean**	**Median**
Match Rights	0.9619		
Days to Match		3.8132	4.0000
Revlon	0.7093		
Premium		0.3292	0.2967
CEO Chairman	0.4236		
Years to Retirement		8.6817	9
Post-Deal Employment	0.5052		
Post-Deal Director	0.0900		
Post-Deal Prestige Job	0.3322		
Passive Market Check	0.4498		
Bids		2.1319	1
Target Initiated First Contact	0.3101		
Pro Acquiror Fiduciary Out	0.9723		
Pro Acquiror Breakup Fee		0.2702	0
Pro Acquiror No Go-Shop	0.9550		
CAR		0.2243	0.2052
Side Payment	0.1697		
Number of Total Contacts		**8.676**	**4**

C. Empirical Analysis

The first prediction is that *Revlon* duties affect the deal process. To test this prediction, I start off by running a simple t-test to see how the relevant deal process characteristics and M&A agreement data are different (as a matter of statistical significance) when a target is in *Revlon* mode as compared to when it is not.

Table 3: *Revlon*'s Effect on Deal Process

Variable	**Mean with Revlon**	**Mean without Revlon**	**Statistical Significance**
Passive Market Check	0.4097	0.5476	0.0344**
Total # Contacts	9.0980	7.6386	0.4894
Pro Acquiror Fiduciary Out	0.9951	0.9167	0.0124**
Pro Acquiror Breakup Fee	0.2272	0.3752	0.1092
Pro Acquiror No Go-Shop	0.9463	0.9762	0.1957
Match Rights	0.9707	0.9405	0.291
Days to Match	3.7854	3.8810	0.5906
Bids	2.2390	1.8795	0.1983

*, **, and *** denote statistical significance at the 10%, 5% and 1% level, respectively.

These results are consistent with Prediction 1 that a target being in *Revlon* mode affects the deal process. In particular, in our sample, targets in *Revlon* mode pursue an active market check about 15% more often than targets outside of *Revlon* mode. The coefficient on the breakup fee variable is not statistically significant; however, it is not far off. Furthermore, its positive value is consistent with intuition—breakup fees tend to be smaller when in *Revlon* mode than not.[139] Interestingly, the coefficient on the fiduciary out variable is a little counterintuitive. Every deal in our sample contains a fiduciary out. However, the results in Table 3 show that when a target is in *Revlon* mode, the deals in our sample are *more likely* to have an acquiror-friendly version of the fiduciary out than when the target is not in *Revlon* mode. This more acquiror-friendly version of the fiduciary out is one that makes it harder for the target to claim a fiduciary out by requiring it to demonstrate not only that the target board's fiduciary duties require consideration of the third-party proposal but also that the third-party proposal is in fact "superior" to the proposal reflected in the target's agreement with the acquiror.

In other words, a target being in *Revlon* mode makes an active market check more likely and decreases the size of the breakup fee, both of which benefit the target. But *Revlon* mode is also associated with contract provisions that benefit the acquiror, making it harder for the target board to avoid recommending the acquiror's deal to the target shareholders.

In some ways, this should not be at all surprising. Negotiating leverage does not simply disappear when negotiating outcomes are affected by legal change. Rather, parties will no doubt assert their given negotiating leverage through other outcomes that are rough substitutes for those outcomes affected by the legal change in question. Thus, *Revlon* clearly makes it more likely that a target, regardless of negotiating leverage, will succeed in prevailing on certain deal process-related negotiating points—including, for example, obtaining an active market check, a modest breakup fee, and a fiduciary out. This is because *Revlon* case law has long expressed a preference for these deal-process characteristics when a target is in *Revlon* mode. However, *Revlon* does not destroy negotiating leverage altogether. Accordingly, one would expect to see acquirors in *Revlon* mode prevailing on other deal-process characteristics about which *Revlon* case law has had very little or nothing to say, like the specific design of the fiduciary out.

Thus, Table 3 is consistent with Prediction 1: *Revlon* mode affects deal process, making targets more likely to secure certain target-friendly deal-process variables like modest breakup fees and active market checks but, at the same time, making acquirors more likely to obtain acquiror-friendly deal process attributes about which *Revlon* case law is more or less silent.

To inspect further the determinants of these various deal process-variables that, according to Table 1, are correlated with whether a target is in *Revlon* mode or not, I ran the logit regression in Table 4 where the dependent variable is the Passive

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139. Remember that the variable is the number of standard deviations away from the sample mean of 3%. Thus, one cannot interpret the difference of the means here as referring simply to differences in the total percentage of the breakup fee. Technically, what these results show is that, in our sample, the breakup fee is about .13 standard deviations closer to the 3% sample mean when the target is in *Revlon* mode than when the target is not. *See supra* Table 3.

Market Check variable, which equals a one if the pre-signing market check is passive and a zero if it is active. The independent variable of interest in this regression is primarily the *Revlon* variable.

Table 4: Determinants of Market Check Decision

	Dependent Variable = Passive Market Check		
Determinant	**Coeff.**	**P-Value**	
Revlon	-0.0169	0.0043	***
Target Initiated First Contact	-0.0475	0.0000	***
CEO Chairman	0.0181	0.0012	***
CEO Stock Option Ownership	0.0000	0.8687	
Years to Retirement	-0.0004	0.9234	
$N = 285$			

*, **, and *** denote statistical significance at the 10%, 5% and 1% level, respectively.

The fact that the *Revlon* variable in Table 4 has a negative coefficient and is statistically significant at the 1% level is consistent with the notion that *Revlon* affects the decision to do an active, rather than passive, market check. This is also consistent with Prediction 1 above.[140]

But Table 4 provides additional color to the decision whether to conduct a passive market check or not. In particular, it suggests that whether the CEO is the chairman or not is also relevant to the decision, because the CEO chairman variable is statistically significant. Moreover, Table 4 suggests that targets whose CEO also serves as the chairman of the board tend to avoid an active market check. Why might this be the case? It seems reasonable to assume that if a CEO has a bias about who to sell the company to, perhaps because of conflicts of interest, then it seems plausible that the CEO will prefer a passive market check to an active one. Bringing in additional bidders under an active market check risks causing the board to prefer some bidder other than the CEO's favored one. The passive market check avoids this possibility. Therefore, the passive market check makes it easier for a conflicted CEO to realize his preferred outcome. But, of course, the CEO does not unilaterally get to decide whether to pursue an active or passive market check. That decision is left up to the board. However, if the CEO is the chairman of the board, then he has a much greater influence over that decision. Thus, this result might be consistent with the underlying story upon which *Revlon* is built—that M&A transactions are fraught with conflicts of interest, and therefore the process must be carefully regulated to ensure that conflicted CEOs and board members act in the shareholders' interests.

Tables 5 and 6 take a similar approach to Table 4, attempting to explain the determinants of the key deal-process variables that, as we saw in Table 3, are affected by *Revlon* mode. In other words, in Table 3, we saw that *Revlon* mode seems to affect certain aspects of the deal process. In Tables 4–6, we are trying to see what factors, in addition to *Revlon*, might explain the variation we see in deal processes.

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140. *See supra* Section II.A.

Table 5: Determinants of Number of Contacts

Determinant	*Dependent Variable = Number of Total Contacts* Coeff.	P-value	
Revlon Mode	-0.0218	0.905	
Passive Market Check	-11.37	0.0000	***
Target Initiated First Contact	1.685	0.381	
CEO Chairman	-0.4442	0.796	
CEO Stock Option Ownership	0.0000	0.160	
Years to Retirement			
N = 276			
Adjusted R-squared = 0.0685			
Regression's P-value = 0.0004			

*, **, and *** denote statistical significance at the 10%, 5% and 1% level, respectively.

Table 5 considers the factors that explain the variation in the number of contacts the target has with bidders, and Table 6 examines the determinants of the number of bids the target receives. In Table 5, the only statistically significant variable that explains the variation in the number of contacts the target has with potential bidders is whether or not the target pursues an active or passive market check. Specifically, an active market check is associated with a greater number of contacts with potential bidders. Table 6 demonstrates that the more contacts a target has with potential bidders, the more bids it receives.

Table 6: Determinants of Number of Bids

Determinant	*Dependent Variable = Number of Bids* Coeff.	P-value	
Revlon Mode	0.2829	0.1611	
Passive Market Check	-0.1407	0.5140	
Target Initiated First Contact	0.6135	0.0043	***
Total Number of Contacts	0.0918	0.0000	***
CEO Chairman	0.2411	0.2058	
CEO Stock Option Ownership	-0.0000	0.2754	
Years to Retirement	0.0028	0.8508	
N = 278			
Adjusted R-squared = 0.4878			
Regression's P-value = 0.0000			

*, **, and *** denote statistical significance at the 10%, 5% and 1% level, respectively.

The story that emerges from Tables 4–6 is this: *Revlon* mode makes it more likely that targets will adopt an active pre-signing market check. And an active pre-signing market check is correlated with a greater number of contacts with potential bidders and a greater number of bids. All of this is consistent with Prediction 1.

But this only raises the question: Do any of these things actually matter in terms of shareholder value? *Revlon* is intended to maximize short-term shareholder value. But it is conceivable that *Revlon* could affect the deal process, as evidenced by the results above, without actually affecting the price that shareholders ultimately get or the market value of the final deal. In other words, does *Revlon* have the effect that is intended? According to Prediction 2, the answer is a resounding "no," since *Revlon*, despite its early billing as an auctioneering duty,[141] really does not operate in that way. As long as a target board follows the preferred *Revlon* process—which is typically an active pre-signing market check combined with a reasonable breakup fee and a fiduciary out—they have considerable latitude in choosing among the merger partners that result from that process.[142] For this reason, Prediction 2 predicts that *Revlon* mode has no effect on the price that target shareholders get or the way the market responds to the announced deal.

To test this prediction, I run a regression of the deal-process variables on two different dependent variables: abnormal market returns upon deal announcement and the premium the deal price represents over market. Thus, the independent variables of interest are the variables relating to whether the deal triggers *Revlon* ("*Revlon*"), whether the target pursued an active or passive pre-signing market check ("Passive Market Check"), the number of contacts the target had with potential bidders ("Number of Contacts") and the number of bids the target received ("Bids"). The control variables include controls for different M&A agreement provisions, target characteristics, deal characteristics, and conflict of interest proxies, all of which are defined in Table 1. This model is very similar to others in the M&A literature, with the exception that in this case I am adding deal-process variables and controls for relevant M&A agreement provisions.[143] The results of these regressions are set forth in Table 7.

The first thing to note is that the estimates for several of the control variables in Table 7 are consistent with the existing M&A literature. For example, I find that the merger premium is lower in deals where the acquiror and target are in the same industry.[144] I also find that the market abnormal returns for the target's stock are increasing with the target's leverage[145] and that these returns are decreasing in deals involving a merger of equals[146] as well as in the target's size as measured by assets.[147] Other studies show that the Merger Premium is higher where there is a breakup fee.[148] The coefficient on our Pro-Acquiror Breakup Fee variable in Table 7 is negative and statistically significant for the regression, where the dependent variable is the Merger

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141. *See supra* text accompanying note 112.

142. *See supra* text accompanying note 120.

143. *See, e.g.*, Fich et al., *supra* note 125, at 348.

144. *Id.* However, it should be noted that their coefficient is not statistically significant.

145. *Id.* Although note that their dependent variable is a measure of deal premium, not abnormal market returns.

146. *See, e.g.*, Cong Wang & Fei Xie, *Corporate Governance Transfer and Synergistic Gains from Mergers and Acquisitions*, 22 REV. FIN. STUDS. 829, 843 (2009); Fich et al., *supra* note 125, at 348, 351 (finding this result for the premium variable and the combined CARS variable—the study does not ever test the target's CARs alone).

147. *See, e.g.*, Fich et al., *supra* note 125, at 348.

148. *See, e.g.*, Bates & Lemmon, *supra* note 100, at 493; Officer, *supra* note 100, at 431.

Premium. This means that shareholders experience negative wealth effects (in terms of market abnormal returns and merger premia) the greater the breakup fee, relative to the sample average of 3%. However, this finding is not necessarily inconsistent with the result in the M&A literature that the Merger Premium is increasing in the size of the breakup fee. In fact, this result is consistent with the intuition that a reasonable breakup fee is efficient (because although it might ward off competing bids, it also attracts bidders), but, at some point, it turns inefficient.

The results also provide some evidence that target firms trade off merger premia in exchange for post-deal employment for the CEO. In regression (2), the coefficient on the variable indicating whether the target CEO receives a Post-Deal Prestige Job—chairman of the board, CEO of the combined company, or CEO of a subsidiary of the combined company—is negative. In other words, the Merger Premium tends to be lower where the CEO is to gain a prestigious post-deal job. This result is consistent with the literature.[149] It is also consistent with the assumption underlying *Revlon*: that the takeover context gives rise to inherent conflicts of interest.

The fact that the estimates for these control variables are either consistent with the literature or consistent with intuition should give us increased confidence in the estimates for our variables of interest, which are the deal-process variables—namely, *Revlon*, Passive Market Check, Bids, and Number of Contacts. The first thing to note about Table 7 is that the estimate for the *Revlon* variable is positive and statistically significant in both of the regressions. That is to say, market returns and deal premia are higher when the target is in *Revlon* mode, everything else equal.

At first blush, this would seem to provide evidence that Prediction 2 is false; in other words, it might appear based on these results that *Revlon* actually does increase shareholder wealth. And indeed, this might be how one interprets other studies that report similar findings.[150] However, one of the main goals of the present study is to try to control for the specific deal process that *Revlon* calls for, something other studies have not done. Once we control for the deal process, the *Revlon* variable is really just a proxy for whether the deal is primarily a cash deal or not.[151] Thus, a correct interpretation of the *Revlon* variable is that market returns and deal premia are greater in *cash* deals. Once again, this is a well-established result in the M&A literature.[152] Many have speculated about why this might be the case, and there is some evidence that cash deals act as a signal to the market that the target is undervalued.[153] However, the effect of cash consideration on market abnormal returns or merger premia does not really tell us anything about whether *Revlon* affects shareholder wealth. In other words, once we control for deal process, the *Revlon* variable does not tell us much, if anything, about Prediction 2.

149. *See, e.g.*, Jay C. Hartzell, Eli Ofek & David Yermack, *What's In It For Me? CEOs Whose Firms Are Acquired*, 17 REV. FIN. STUDS. 37, 52–53 (2004).

150. *See supra* notes 125–34 and accompanying text.

151. To be sure, the *Revlon* variable also seeks to capture control transactions. But as explained earlier, the vast majority of the deals captured by this variable are non-control cash deals, where a cash deal is defined as 50% cash or more. *See supra* notes 128–35 and accompanying text.

152. *See supra* notes 125–34 and accompanying text.

153. *See, e.g.*, Malmendier et al., *supra* note 125, at 92.

Nevertheless, one might reasonably question whether this interpretation of the *Revlon* variable is actually correct. One might entertain such a thought—particularly if one thinks that *Revlon* duties are not just process-oriented but still retain some substantive bite. This would be true, for example, if *Revlon* really did meaningfully constrain the target board's choice of merger partner from among the bidders generated by the *Revlon* process. In other words, it could be true that our *Revlon* variable continues to capture some effect of the *Revlon* doctrine (despite controlling for the *Revlon* process) if, for example, pursuant to the original conception of the "auctioneering duty," the target board really did have to choose the highest bidder. I argued in Part I that this is not how the modern application of *Revlon* works in practice.

But one might be skeptical of such a claim. For that reason, I include in the model in Table 7 the interaction variable "Bids*Revlon*." The estimate of this variable should be interpreted as the effect the number of bids has on market returns and merger premia when the target is in *Revlon* mode. If *Revlon* retains some substantive bite above and beyond its effect on the deal process, one would expect the coefficient on this interaction variable to be positive and statistically significant. However, it is neither of these. This result is thus consistent with the view, expressed in Part I, that *Revlon* lacks much, if any, substantive bite. Although *Revlon* affects the sales process the target board undertakes, it does not affect how a target ultimately decides among the choices the process generates. In other words, the effect that the number of bids has on market returns and deal premia is no different in *Revlon* mode than outside of *Revlon* mode, and outside of *Revlon* mode, the standard is the business judgment rule, which is highly deferential to the target board's decision. The interaction variable's lack of statistical significance indicates that courts are similarly deferential to the target board's decision as to a merger partner, even within *Revlon* mode. And for this reason, it is reasonable to interpret the *Revlon* variable as a proxy for whether the deal is for cash or stock.

To be clear, however, the fact that *Revlon* lacks substantive bite, consistent with our review of the case law in Part I and the lack of statistical significance of the interaction variable in Table 7, does not in and of itself mean that *Revlon* has no effect on shareholder wealth. After all, it has already been shown that *Revlon* has real effects on the sales process, and the sales process itself could affect shareholder wealth even though *Revlon* does not appear to require the board to decide among the results of that process any differently than outside of *Revlon*. In other words, even though the interaction variable might not be statistically significant, it still might be the case that market returns and premia are higher the more bids the target attracts. And, if as has already been shown, *Revlon* affects the number of bids through its preference for an active pre-market check, then it could still be the case that *Revlon* affects shareholder wealth. However, as one can see from Table 7, besides one exception, none of the estimates for any of the deal-process variables, other than the *Revlon* variable itself, are statistically significant. Put differently, this is evidence that deal process does not matter for shareholder wealth, whether one is in *Revlon* mode or not.[154]

154. The one exception is the estimate for the variable relating to the Total Number of Contacts. This estimate is negative and statistically significant for regression (1) involving the

Table 7: Determinants of Short-Term Shareholder Returns

Regression:	(1)			(2)		
Dependent Variable:	CAR (-1, +1)			Premium		
	Coeff.	**P-value**		**Coeff.**	**P-value**	
Deal Process Characteristics						
Bids	-0.0005	0.9654		-0.0375	0.7845	
Revlon	0.1425	0.0002	***	0.0922	0.0797	*
Bids**Revlon*	-0.0079	0.5016		0.0089	0.5867	
Passive Market Check	0.0138	0.5930		0.0252	0.4896	
# Total Contacts	-0.0020	0.0722	*	-0.0011	0.4528	
Conflict of Interest Variables						
CEO Chairman	0.0248	0.2962		0.0210	0.5282	
Years to Retirement	0.0013	0.4858		0.0007	0.7918	
Post-Deal Director Only	-0.0584	0.1561		-0.0705	0.2246	
Post-Deal Prestige Job	-0.0296	0.2307		-0.0842	0.0164	**
Side Payment	0.0245	0.4112		0.0087	0.8346	
M&A Agreement Data						
Pro Acquiror Fiduciary Out	0.0233	0.7324		0.1655	0.1016	
Pro Acquiror Breakup Fee	-0.0393	0.0564		-0.0482	0.0928	*
Pro Acquiror No Go-Shop	-0.0237	0.6479		0.0652	0.3830	
Days to Match	0.0102	0.2290		0.0179	0.1698	
Target Characteristics						
Size	-0.0001	0.0000	***	-0.0001	0.1342	
Leverage	0.0962	0.0914	*	0.2929	0.0005	***
M/B	0.0002	0.6573		-0.0005	0.5410	
OCF	-0.0072	0.9215		0.4630	0.6532	
Deal Characteristics						
Tender Offer	0.0189	0.5435		0.3572	0.4153	
Same Industry	-0.0368	0.1107		-0.0724	0.0253	**
Merger of Equals	-0.1246	0.1000	*	0.0356	0.7402	
N =	241			235		
Adjusted R-squared =	0.19			0.09		
Regression's P-value =	0.0000			0.0036		

*, **, and *** denote statistical significance at the 10%, 5% and 1% level, respectively.

market-returns variables, but not statistically significant for regression (2) involving the deal premium dependent variable. This estimate seems to show that market returns are actually lower the more potential bidders a target talks to, with no effect on the deal premium. How might we explain this? One possibility is that targets who know that a sale will be relatively unpopular to shareholders, perhaps because shareholders believe that the target is currently undervalued by the market, intentionally talk to more potential bidders in an effort to placate the shareholders. This then allows them to better defend the sale in their SEC disclosure by touting the number of potential bidders contacted. This Article does not explore in any detail whether this hypothesis is true because it seems, at best, tangential to the current inquiry.

D. Objections and Extensions

One potential objection to Table 7 might be that in our second regression equation—where the dependent variable is the market premium—there is an endogeneity problem since the market premium and the deal process variables are jointly determined. In other words, the deal process affects the price, but it is also affected by price, in which case the estimates of our deal process variables are unreliable. However, the first equation—where the dependent variable is market returns—acts as a control for endogeneity, since the market reaction is not determined until after the deal process has been put into effect.[155] The fact that the first equation's result confirms the results of the second equation serves as a robustness check.

Another potential objection to the foregoing empirical results is that my focus on deal process ignores the potential effect that *Revlon* has on effort. After all, one factor that courts often take into consideration in analyzing a board's compliance with their *Revlon* duties is how "hard" the target board negotiated.[156] This effort variable could be measured by the number of counteroffers that are made with the winning bidder or the difference between the winning bidder's opening and ending bids. It is entirely possible that the picture painted here is true: *Revlon* affects certain aspects of the deal process, but those aspects do not affect shareholder returns, and, at the same time, *Revlon* increases shareholder returns through its effect on how hard target boards negotiate.

In fact, based on the evidence presented here, this result is not only possible but likely. After all, it seems likely that *Revlon* affects how hard target boards negotiate since it affects all other aspects of deal process that are a focus of the present study. There seems to be little question that the Delaware courts, as well as deal lawyers representing target boards, do a good job of communicating to boards the need to follow a particular process when in *Revlon* mode.[157] And there is no reason to believe that *Revlon*'s insistence on "hard negotiating" would be any different.

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155. In a contemporaneous paper, Matt Cain, Steven Davidoff Solomon, and their co-authors find that whether a company is in *Revlon* mode is correlated with higher premiums. Cain et al., *supra* note 132. Contrary to the approach taken here, they do not re-run their regression with market returns as the dependent variable. *Id.* Instead, they attempt to solve the endogeneity problem by running the same regressions in states other than Delaware. *Id.* They find that *Revlon* mode is not associated with higher premiums in these non-Delaware states, a finding that they regard as evidence that it is really the peculiarities of Delaware law that accounts for their results and not something else, like the possibility that higher premiums are also associated with cash deals irrespective of the law. *Id.* This is an interesting result, but it is also somewhat puzzling since, as others have noted, many non-Delaware states adopt *Revlon* as their law, including particularly significant ones like California. *See, e.g.*, Michal Barzuza, *The State of State Antitakeover Law*, 95 VA. L. REV. 1973, 2012 (2009). For these reasons, among others, I tend to view their different results as having less to do with better endogeneity controls and more to do with the date range of their data set, which takes into account the early 2000s merger boom when *Revlon* likely worked differently and had more substantive bite than after 2009, the period focused on here. *See supra* note 130 and accompanying text.

156. *See supra* note 98 and accompanying text.

157. Letter from J. Anthony Terrell, Att'y, Pillsbury Winthrop Shaw Pittman LLP, to Clients and Friends (May 11, 2016), https://www.pillsburylaw.com/images/content/1/0

Additionally, unlike the other deal process variables focused on here, "negotiating effort" is not as affected by the relatively recent *Revlon* cases, like *In re Family Dollar Stores, Inc. Stockholder Litigation*[158] and *C&J Energy Services*,[159] which have arguably defanged much of the substantive and procedural bite of the earlier incarnations of the *Revlon* doctrine. By clarifying that *Revlon* does not require the target board to choose, or even negotiate with, the highest bidder, *Family Dollar* weakened *Revlon*'s substantive bite.[160] By holding that *Revlon* does not require any sort of active solicitation, even if the target board's knowledge of the market is less than "impeccable," *C&J Energy Services* weakened *Revlon*'s procedural bite.[161] Together, these developments give reason to question whether the deal process variables included in the foregoing regressions will ultimately affect shareholder returns. Even if a target board adopts an active solicitation process, *Family Dollar* gives them considerable latitude to partner with their preferred bidder.[162]

However, this is not the case with respect to "negotiating effort." There is no reason to believe that cases like these would affect a board's negotiating effort. Furthermore, it stands to reason that the harder a board negotiates with the winning bidder, the higher the price will be, assuming that it does not negotiate too hard and chase the bidder away. Thus, it is also reasonable to assume that measures of shareholder return, including abnormal market returns upon deal announcement and deal premia, will be increasing with negotiating effort. For these reasons, *Revlon* likely affects how hard a target board negotiates, and negotiating effort is likely associated with higher shareholder returns.

However, even if this is true, the overall picture that this study paints of *Revlon*'s effect on deal process would remain intact. Even if the Court's modern *Revlon* jurisprudence does not diminish a target board's negotiating effort when in *Revlon* mode, it allows the target board to decide with which bidders to apply such effort. And that decision could be motivated by conflicts of interest that courts applying *Revlon* typically ignore, things like side payments and post-deal employment. For this reason, the failure to include a measure of negotiating effort does not affect the overall thrust of this Article, which is the need to re-orient the *Revlon* doctrine around the original conflicts of interest rationale that motivated the doctrine in the first place. This is the topic of the next Part.

III. Policy Discussion

The empirical results confirm our hypothesis that *Revlon* duties do not really matter for shareholder value. To be sure, these results confirm that *Revlon* affects deal process in all of the ways one would expect: it increases the use of active pre-signing market checks, it increases the number of potential acquirors the target talks to, and it increases the number of bids received. Nevertheless, these aspects of the deal process do not ultimately appear to affect the premium received by target

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/104200.pdf [https://perma.cc/Y96W-W8YS].

158. No. 9985-CB, 2014 WL 7246436 (Del. Ch. Dec. 19, 2014).

159. 107 A.3d 1049 (Del. 2014).

160. *See* 2014 WL 7246436, at *16.

161. 107 A.3d at 1069.

162. *See* 2014 WL 7246436, at *23.

shareholders or the value that the market places on the deal. The reason for these phenomena most likely has to do with the fact that, despite the stated reasons underlying *Revlon*'s heightened standard of review, *Revlon* duties are not effectively designed to address conflicts of interest.

A. Revlon's *Lack of Fit Between Problem and Solution*

Although there might not be a single blueprint for *Revlon*, as we have seen, there are certain blueprints that are more likely to pass muster than others. For example, a target firm that adopts an active pre- or post-signing market check combined with a fiduciary out and termination fee in the 3% range will almost certainly satisfy *Revlon*. And yet, on reflection, this description of what *Revlon* requires should be a little puzzling. After all, it does not seem that *Revlon* duties are particularly well tailored to the problem at the heart of *Revlon*, which, as discussed in Part I, is the conflicts of interest inherent in the sale decision.

There are generally two ways of solving conflict of interest problems. First, one can try to neutralize the conflicts. For example, a conflicted officer or director could recuse herself from the board's decision-making with respect to the issue that presents the conflict in the first instance. Second, one could introduce another layer of substantive review by an objective arbiter, for example a court, board, or the shareholders, to review a conflicted decision that has already taken place. This two-prong approach is how Delaware courts treat typical conflict of interest issues under the duty of loyalty.[163] If the board that authorizes the conflicted transaction is conflict-free because any conflicted directors have recused themselves from the decision-making, then the board's decision is subject to the highly deferential business judgment standard. The same is true if the decision, though not free of conflict, is ratified by a disinterested board or disinterested shareholders. Otherwise, a court will review the substantive and procedural fairness of the decision.

Revlon does not take this approach. Rather, *Revlon* has developed in such a way that one might be forgiven for thinking that the problem it is trying to solve has less to do with conflicts and more to do with a lack of care. To be clear, the Delaware Chancery Court has clarified that "*Revlon* duties are only a specific application of directors' traditional fiduciary duties of care and loyalty in the context of control transactions."[164] In other words, *Revlon* has to do with both care and loyalty. This makes sense because conflicts of interest can cause a lack of care. For example, a chairman who is offered a lucrative post-deal consulting position by a bidder might be induced to adopt a less than thorough process in order to justify accepting the bidder's offer. Thus, there is little question that the duty of care is relevant to *Revlon*. But the point is that at bottom, the concern is one of a conflict of interest.[165]

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163. *See, e.g.*, In re Pilgrim's Pride Corp. Deriv. Litig., 2019 WL 1224556, at *15 (Del. Ch. Mar. 15, 2019) ("A director can avoid liability for interested transaction by totally abstaining from any participation in the transaction"); Benihana of Tokyo, Inc. v. Benihana, Inc., 906 A.2d 114, 120-21 (explaining that when a conflicted transaction is approved by disinterested directors the court is to defer to the board under the business judgment rule).

164. Dent v. Ramtron Int'l Corp., No. 7950-VCP, 2014 WL 2931180, at *5 (Del. Ch. June 30, 2014).

165. This suggests that liability under *Revlon* should never be exculpable under a Delaware

If *Revlon* was solely about a lack of care, then *Revlon*'s solution—mandating certain procedural features—would make sense. But that only works if we think that the fiduciaries are simply shirking rather than acting out of self-interest. If the problem is really one of a conflict of interest, then that problem is still going to be there no matter how much process is layered on.

For example, consider a situation where the CEO's wife, a well-known opera singer, is being considered by the company to headline a new opera-themed marketing campaign.[166] The typical way to deal with that conflict of interest would be either to require the CEO to recuse himself from the board's decision-making or to have a court determine whether the deal with the CEO's wife is entirely fair. It would not do to simply add additional process—for example, requiring the board to canvas the market for opera singers if, at the end of that canvassing, the board could give in to the conflicts and hire the CEO's wife without having to defend the substantive fairness of that decision. And yet, that is effectively what *Revlon* requires.

The odd fit between the conflicts of interest that *Revlon* seemingly intended to address and the process that it requires implies that a conflicted target board could effectively select the bidder toward which its conflicts prejudice it as long as the target board simply checks the relevant *Revlon* process boxes. In other words, one legitimate concern with *Revlon* is that it does not mitigate but instead exacerbates the conflict of interest problem by creating a process-based safe harbor that does not in itself prevent the conflicts that risk prejudicing the board's decision.

The empirical evidence reported in Part II is consistent with this story.

B. Policy Choices: More Robust Conflict Review, More Shareholder Disclosure

1. More Robust Analysis of Target Board Conflicts

The policy options basically follow from the two-pronged framework Delaware adopts for dealing with conflicts of interest, as reviewed above. First, consistent with Delaware's approach to conflicts of interest, one could focus on neutralizing the conflict at issue. If the choice of merger partner is made by a disinterested board and the deal process looks reasonable, then courts should defer to that decision. Indeed, the Delaware courts already understand themselves to be doing something precisely along these lines in the *Revlon* context. For example, in *Family Dollar*,[167] the Delaware Chancery Court observed that "when the record reveals no basis to question a board's motivations, the Court understandably will be more likely to defer

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Code § 102(b)(7) provision. Yet, courts do not typically analyze *Revlon* claims by assuming that at bottom, if *Revlon* applies, it is because of a conflict of interest. Rather, they view it in terms of the reasonableness of the target board's actions. And thus, the question is whether the board acted with a conscious disregard of their duties, in which case the duty of loyalty is implicated. Otherwise, they dismiss the claim on account of the § 102(b)(7) provision. *See, e.g.*, Lyondell Chem. Co. v. Ryan, 970 A.2d 235, 239–40 (Del. 2009).

166. This is an obvious allusion to the famous case of *Bayer v. Beran*, 49 N.Y.S.2d 2 (N.Y. 1944).

167. 2014 WL 7246436.

to the board's judgment in determining how to conduct a corporate sale process."[168]

However, there are at least two problems with the current approach. First, the evidence in Part II does not imply that process does not matter at all. Rather, it implies that a particular sales process is not a sufficient condition for maximizing short-term shareholder returns, particularly if the courts are not going to police how target firms select among the bidders generated by that process.[169] However, process still matters. Courts are never going to be able to perfectly identify when a board is completely free of conflicts because some conflicts are not readily identifiable. The process a board chooses, however, can be indirect evidence of conflicts. Specifically, the choice of an entirely passive sales process when the board lacks considerable knowledge of the market should constitute such indirect evidence of a conflict of interest. For this reason, I view *C&J Energy Services* as a mistake to the extent that it overturns *Barkan* and its progeny's presumption in favor of an active solicitation process unless the target board has "impeccable knowledge" of the market.[170]

However, even with a good sales approach, there might be lurking conflicts of interest that prevent the target board from selecting the bidder that would maximize shareholder returns, and it is not clear that the courts always engage in a sufficiently robust conflicts review. This is the second problem with the current approach courts take with respect to *Revlon*. As a general matter, courts apply different levels of scrutiny when analyzing board conflicts, and they often do so without explaining why. Take, for example, the context of the special litigation committee, the board committee established to determine whether the corporation should cause a shareholder derivative lawsuit to be dismissed. In a case like the well-known *Auerbach v. Bennett*,[171] the court deemed the committee disinterested because its directors were not board members at the time of the transaction that gave rise to the underlying lawsuit.[172] Yet, in a case like *In re Oracle Corp. Derivative Litigation*,[173] this same fact did nothing to prevent the court from concluding, after a much more searching review, that the committee was conflicted.[174] In the *Revlon* context, Delaware courts generally seem to prefer a very light sort of *Auerbach* review, whereas it would be more consistent with the origins of *Revlon* to perform the type of searching review one sees in *In re Oracle*.

To illustrate, consider the *Family Dollar* case.[175] Family Dollar entered into a merger agreement with Dollar Tree at a price of $74.50 in cash and stock.[176] It did so at a time when it was in ongoing negotiations with a different bidder, Dollar

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168. *Id.* at *12.

169. I'm not suggesting that the courts should, but they've made it pretty clear that they will not. *See id.*

170. *See* C&J Energy Servs., Inc. v. City of Miami Gen. Emps.' & Sanitation Emps.' Ret. Tr., 107 A.3d 1049, 1068–71 (Del. 2014)*; see also In re* OPENLANE, Inc. S'holders Litig., No. 6849-VCN, 2011 WL 4599662, at *5 (Del. Ch. Sept. 30, 2011).

171. 303 N.E.2d 994 (N.Y. 1979).

172. *See id.* at 997.

173. 824 A.2d 917 (Del. Ch. 2003).

174. *See id.* at 929.

175. *In re* Family Dollar Stores, Inc. S'holders Litig., No. 9985-CB, 2014 WL 7246436 (Del. Ch. Dec. 19, 2014).

176. *Id.* at *1.

General, which seemed “anxious to do a transaction” but who was never informed of the discussions between Family Dollar and Dollar Tree because of a non-disclosure agreement between those two parties.[177] Shortly after the deal between Family Dollar and Dollar Tree was announced, Dollar General made a bid of $80 per share in cash, which the Family Dollar board rejected.[178] In the subsequent lawsuit, where Dollar General alleged a *Revlon* claim, the court determined that the Family Dollar board was not conflicted because the majority of the board consisted of outside directors and many of them had a lot of stock in the company.[179] After the lawsuit, Family Dollar had to adjourn its shareholders meeting because it did not have sufficient support among its shareholders to ensure approval of the merger with Dollar Tree because of the possibility of Dollar General’s higher bid.[180]

Thus, the *Family Dollar* court’s conflicts review largely focused on whether the board consisted of outside directors or not.[181] However, the types of concerns over conflicts that animate *Revlon* could occur even on a board consisting of a majority of outside directors and even among those with a lot of money on the line. In fact, the plaintiffs in *Family Dollar* made allegations of such conflicts, arguing that Howard Levine, the chairman of the company and son of its founder, who was charged with negotiating the deal, preferred the Dollar Tree deal because of an expressed desire to be part of the combined company and because of Dollar Tree’s apparent willingness to keep the company headquarters in its current location in North Carolina.[182] However, the court gave these arguments short shrift, viewing them as mere negotiating tactics that did not reflect Levine’s true views.[183] One piece of evidence in support of the view that headquarters location was an important consideration in the choice of bidder was an email sent to Levine by one of his directors, who also happened to be North Carolina’s Secretary of Commerce, in which she expressed her conditional support for the deal as long as the headquarters remained in North Carolina.[184] The court treated this email from a person whose elected position required her to advocate for North Carolina’s business interests as an obvious joke since the email ended with a smiley face.[185]

The Delaware Supreme Court’s approach to board conflicts in *C&J Energy Services*[186] was similarly limited but perhaps even more revealing. There, then-Chief Justice Strine suggested that the benchmark for a conflicts analysis should come from the facts of *Revlon* itself, which involved “a decision by a board of directors to chill the emergence of a higher offer from a bidder because the board’s CEO disliked the

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177. *Id.* at *3–4.

178. *Id.* at *9–10.

179. *Id.* at *13.

180. *Family Dollar Adjourns Shareholder Meeting On Dollar Tree Deal*, REUTERS (Dec. 23, 2014), https://www.businessinsider.com/r-family-dollar-adjourns-shareholder-meeting-on-dollar-tree-deal-2014-12 [https://perma.cc/9L7Y-RR2Y].

181. *Family Dollar*, 2014 WL 7246436, at *13.

182. *Id.* at *2, *13.

183. *Id.* at *13.

184. *Id.*

185. *Id.*

186. C&J Energy Servs., Inc. v. City of Miami Gen. Emps.’ & Sanitation Emps.’ Ret. Tr., 107 A.3d 1049 (Del. 2014).

new bidder."[187] Short of that type of conflict, the Chief Justice implied, the board should be deemed independent, as the court found in *C&J Energy Services*.[188]

This approach strikes me as taking too narrow a view of potential board conflicts, particularly in light of the concerns underlying *Revlon*. Those concerns were not simply that the target CEO might not like the CEO of one of the bidders, which seems like a rather unusual conflict actually. The more common source of conflict, one would think, derives from interests that the CEO, chairman, or whoever is leading the negotiation on the part of the target has in the merger. Accordingly, a more robust analysis of target board conflicts in this context would consider a number of different factors, including how the deal process was decided; whether it was influenced by the person who was negotiating with the bidder on behalf of the target; whether that negotiator, or anyone else involved in the decision, had anything to gain from going with one particular bidder over another; and whether that potential conflict materialized at a point during the course of negotiations that it could have influenced the ultimate outcome. For example, one could imagine a scenario where the CEO, who negotiated the deal, is to receive a "transaction bonus" from the bidder but that the bonus was not broached by the bidder until after the board had already selected that bidder for other reasons.

Finally, the *C&J Energy Services* court's conflicts review was lacking in a different respect. It failed to acknowledge what was implicit in the lower court opinion—the target board's lax sales process itself raised the specter of conflicts even if no obvious conflicts could be identified.[189] This was the wisdom of the *Barkan* court's strong preference for an active sales process with only a very limited exception for situations where the target board already had a high degree of knowledge about the market.[190] We would do well to return to that *Barkan* standard while engaging in a more searching conflict review than the ones we see in either *Family Dollar* or *C&J Energy Services*.

2. More Shareholder Disclosure

In the Delaware approach to conflicts, an alternative to neutralizing the conflict would be to have the conflicted transaction ratified by a fully informed disinterested party, like shareholders. This appears to be the approach recently taken in *Corwin v. KKR Financial Holdings LLC*, where the Delaware Supreme Court held that the business judgment rule—and not *Revlon*'s heightened standard—is the appropriate standard of review in a post-closing damages suit involving a merger that has been approved by a fully informed, uncoerced majority of disinterested shareholders.[191] In other words, according to the *Corwin* court, the target shareholder vote, which is required by the Delaware corporate law statute, can also serve to ratify any lapse under *Revlon*.[192] This raises a number of issues, for example, the possibility that the

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187. *Id.* at 1067.

188. *Id.* (opining that understanding the nature of this conflict in *Revlon* is important to understanding the case and everything that has come after it).

189. *Id.* at 1052–53.

190. Barkan v. Amsted Indus., Inc., 567 A.2d 1279, 1286–87 (Del. 1989).

191. 125 A.3d 304, 306, 308 (Del. 2015).

192. *Id.* at 308.

choice given to shareholders might be distorted particularly in situations where the board had little time to pursue other potential bidders.[193] Although these types of concerns are always present when it comes to shareholder ratification of board conduct, they might be of heightened relevance in this context.

However, another issue is one of information. In determining whether to accept the bird in the hand over the one in the bush, shareholders need to know whether the board's decision to accept the acquiror's offer is free of conflict. Current securities disclosure rules are not as clear as they might be on that score. True, federal securities laws require the target to disclose any interests that the directors or officers might have in the merger.[194] However, no disclosure is required if the interest has not yet materialized, and therefore acquirors can get around these disclosures with a wink and a nod, promising the chairman or CEO a transaction bonus or some other type of merger side payment but not before the proxy statement goes out. For example, disclosures sometimes identify a pool of money that is to be paid out in transaction bonuses but has not been distributed by the time the proxy statement is circulated. Consequently, there is no way of knowing whether the person who negotiated the deal is included among the potential recipients of that money. Disclosure of any expectations of side payments would help address this issue.

Additionally, merger side payments are not necessarily always bad. They might, for example, be necessary in order to persuade a reluctant CEO to relinquish the reins of the company and his position, along with the accompanying perks, to a more efficient acquiror. In this sense, merger side payments can be a way of addressing deficiencies in the structure of a CEO's golden parachute compensation. There is even some evidence to this effect.[195] For this reason, it would be useful to include in the disclosure the reason for any merger-related side payment.

Post-deal employment is another issue. Like merger side payments, the fact that the CEO, chairman, or other officers of the target will be employed by the acquiror in some respect following the transaction is not in and of itself a bad thing. Some acquirors, like Warren Buffett's Berkshire Hathaway, pride themselves on making very few, if any, governance changes post-acquisition, including keeping CEOs at the helm.[196] Sometimes the CEO or chairman is central to the value proposition the acquiror sees in the target. Other times, post-deal employment is simply a carrot extended to the CEO or chairman to accept that particular acquiror's bid.

Two potential disclosure rules could help address these concerns. First, the target should have to disclose at what point during the negotiations the lead negotiator on behalf of the board discovered that he or she might be offered a position in the combined company. Some boards are careful to try to reserve any such discussions until after the bid has been accepted. But this does not happen all of the time. Second,

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193. *See, e.g.*, Cox & Thomas, *supra* note 73, at 340.

194. *See* Information Required in Proxy Statement, 17 C.F.R. §240.14a-101, Item 5 (2018).

195. *See, e.g.*, Fich et al., *supra* note 125, at 340 ("Our evidence is consistent with the view that a merger bonus is typically used to mitigate conflicts of interest between target CEOs and their shareholders.").

196. Shana Lynch, *What Is It Like to Be Owned by Warren Buffet?*, INSIGHTS BY STANFORD BUS. (Oct. 29, 2015), https://www.gsb.stanford.edu/insights/what-it-be-owned-warren-buffett [https://perma.cc/QZK5-9KRB].

the target should have to disclose the reason why the acquiror wants to retain the CEO, chairman, or other person responsible for negotiating the deal on behalf of the target; why those attributes are unique or could not be easily captured by someone currently employed or otherwise known by the acquiror; and whether the acquiror has a policy of retaining such persons and has done so with respect to other acquisitions.

CONCLUSION

In this Article I have argued that, given the way the *Revlon* doctrine has developed over time, one should not expect that *Revlon* achieves what it was originally designed to achieve: maximizing short-term shareholder wealth. I have also presented evidence supporting this argument. Finally, I have suggested that to fix *Revlon*, we might bring the doctrine more in line with the way Delaware law typically addresses conflict of interests: a more robust review of potential conflicts and greater disclosure of such conflicts.

To be sure, I am not suggesting that such policy proposals, if adopted, would solve the problem at the heart of *Revlon*. Conflicts of interest are complicated because they are not unequivocally bad, and attempts to eradicate all conflicts, I suspect, would do more harm than good. Nor do I think the theoretical and empirical criticisms of *Revlon* presented here should cause one to conclude that the doctrine is completely useless and could be scrapped without consequence. Just as we think that the shareholder welfare maximization norm does not need to be enforced to be valuable,[197] the same might be true of *Revlon*. Nevertheless, the doctrine does not appear to do what people assume it does. And that's a fact that needs to be reckoned with for the future of corporate law.

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197. This would be the justification of famous cases like *Shlensky v. Wrigley*, 237 N.E.2d 776 (Ill. App. Ct. 1968), where the court extols the shareholder maximizing norm but then applies a robust form of the business judgment rule.